



Opportunities and Constraints for Civil Service Reform in Indonesia

Exploration of A New Approach and Methodology

The contents of this report is financed by an ASEM grant to the Government of Indonesia, administered by the World Bank jointly disseminated by the World Bank and the Partnership for Governance Reform in Indonesia

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ISBN : 979-26-9606-7

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Joint publication of the World Bank and
the Partnership for Governance Reform in Indonesia

TABLE OF CONTENT

GENERAL INTRODUCTION

CHAPTER 1: IDENTIFICATION OF CONSTRAINTS AND OPPORTUNITES FOR CIVIL SERVICE REFORM AT THE REGIONAL LEVEL

CHAPTER 2: CIVIL SERVICE REFORM: REGIONAL PERSPECTIVES

- WEST NUSA TENGGARA
- WEST SUMATRA
- METHODOLOGY USED
- PROPOSED PILOT IN KOTA SOLOK, WEST SUMATRA

CHAPTER 3: FINANCIAL ISSUES IN CIVIL SERVICE REFORM

CHAPTER 4: POSSIBLE FOCUS AND ORGANIZATION OF CENTRALLY DRIVEN REFORM INITIATIVES

CHAPTER 5: LESSONS FROM INTERNATIONAL GOOD PRACTICE

CHAPTER 6: KEY ASPECTS OF THE INDONESIAN SITUATION

CHAPTER 7: IDENTIFICATION OF MAJOR POLICIES AND TECHNICAL INSTRUMENTS FOR REFORM OF PERSONNEL AND ORGANIZATION; REVENUE AND EXPENDITURE

ANNEXES

GENERAL INTRODUCTION

The World Bank has been administering on behalf of the government of Indonesia, an ASEM grant which aims to develop a *Methodology for Regional Civil Service Reform*. Within the prevailing complicated legal, institutional and regulatory framework, the work program financed by the ASEM grant has developed recommendations aimed at alleviating the serious constraints caused by the administrative, personnel and financial regulations imposed on regional governments. At present these constraints are impeding the efficient and effective improvement of service delivery and other functions that needs to be reformed.

The program has been completed and this volume contains two reports intended to disseminate the results and findings. The first report is entitled: ***Constraints and Opportunities for Civil Service Reform in Indonesia: Exploration of a New Approach and Methodology***. The second report is entitled: ***Innovation in the Regions: a New Initiative for Kota Solok***. The latter describes a proposed pilot in detail, including its rationale, purpose and Terms of Reference. At the time of printing it had not yet been confirmed when the pilot would commence but stakeholders in government as well as donors have shown a keen interest in the proposal.

This volume highlights and summarizes various previous reports, briefing notes and summaries of meetings and workshops produced during the implementation of the work program of the ASEM grant. Four earlier reports on part of the work program have already been issued. Two were published by the World Bank: these are *Civil Service Reforms at the Regional Level: Institutional, Regulatory and Financial Issues facing Reforming Regions in Indonesia* (July 2005) and *Completed Civil Service Diagnostics and Road Maps for Reform in Nusa Tenggara Barat* (July 2005). Two other reports were issued and distributed but not published by the World Bank: *Completed Civil Service Diagnostics and Road Maps for Reform in West Sumatra* (October 2005) and *Synthesis Report*. The latter comprises of three parts: Part 1 – *Major Policies and Technical Instruments for Reform of Personnel and Organization; Revenue and Expenditure*; Part 2 – *Civil Service Reform in Regions' Contents of a Pilot Project*; Part 3 – *Possible Focus and Organization of Centrally Driven Civil Service Reform Initiatives*.

The purpose of this volume is to inform a broad audience about the results of the study and in particular to share the methodology and its results in the hope that the latter may contribute to a more favorable environment for civil service reform. In addition, work done under the auspices of the grant has aimed to raise awareness about the current state of the civil service in Indonesia and the problems and options for reform, and thereby to stimulate and motivate reform minded officials in central government, and in particular in the regions, to continue the debate and to exert pressure for urgently needed reforms.

This publication and materials related to the study can also be consulted and downloaded at a newly created website, www.civilservicereform.org, currently under development by the Partnership for Governance Reform in Indonesia and in cooperation with the World Bank. This website will create a permanent, interactive platform for discussing civil service reform issues in general, as well as presenting the results of this study and future program.

The disseminating of the results of this study takes place at an important moment. Various initiatives related to civil service reform are currently under development (see Chapter 5), in particular a Presidential initiative to start a comprehensive reform process and the activities of the Corruption Eradication Commission (KPK). The emerging comprehensive reform agenda under the auspices of the President is compatible with the suggestions in this volume that reforms must be driven by the top political leadership if reform is to be successfully realized.

Explanatory note to the reader

The study was conducted in two phases: an analytical phase and a field work phase. The phases comprised four steps.

Step 1: To identify and analyze the opportunities and constraints facing regions as they attempt to carry out civil service reforms. This work resulted in the publication: *Civil Service Reforms at the Regional Level: Opportunities and Constraints: Executive Summary*, World Bank 2005. This summary was written from the perspective of the reforming regions and is based on documentation and interviews with relevant actors at the national and regional levels.

Step 2: To conduct field studies in West Nusa Tenggara (NTB) and West Sumatra (carried in 2005). The field study in NTB was published by the World Bank: *Completed Civil Service Diagnostics and Road Maps for Reform in Nusa Tenggara Barat* (July 2005). (The report on West-Sumatra has been widely distributed but has not been published.)

Step 3: To identify key reform areas, propose a pilot to address key reform areas in a selected local government; and assess of the likelihood that GOI will undertake centrally driven reform. This work resulted in a synthesis report, which has not been published.

Step 4: To disseminate the results of the three previous stages in two reports: Report number one – *Opportunities and Constraints for Civil Service Reform in Indonesia: Exploration of a New Approach and Methodology*. Report number two – *Innovations in the Regions: A New Initiative for Kota Solok*.

Both reports aim to be useful to a wide audience. Parts of the texts have been written in a checklist format in order to be user-friendly for decision-makers and implementers of reforms. Teams of consultants have produced the reports under the guidance of the World Bank and GOI, but the views and judgments of the report are those of the consultants, and do not reflect the official views of the World Bank, the Government of Indonesia or the Partnership for Governance Reform in Indonesia.

CHAPTER 1

IDENTIFICATION OF CONSTRAINTS AND OPPORTUNITIES FOR CIVIL SERVICE REFORM AT THE REGIONAL LEVEL

Institutional and Regulatory Issues

Section A. The Regulatory Environment

The central regulatory environment is characterized by the large number of agencies that share responsibility for managing the national and regional civil services: BKN (National Civil Service Agency); Menpan (State Ministry for State Apparatus Reforms); Ministry of Home Affairs; LAN (National Institute of Administration); Ministry of Finance; *sectoral* ministries; and regional (provincial, district and city) governments. All have responsibilities for oversight and/or regulation, policy-making, line management and technical assistance and training.

The definition of respective responsibilities, however, has never been completely clear; a 1993 World Bank study described the regulatory framework as fragmented and blurred and stated that agencies were neither performing their respective functions adequately nor ensuring coherent coordination among themselves. The mandates of BKN and Menpan; for example, reveal considerable overlapping and both appear to be involved in crucial tasks such as guidelines for the preparation of the *formasi*, recruitment and the recent census.

Many observers have documented and analyzed the long-standing absence of effective management of the civil service which is rooted in the complexity and ambiguities of the regulatory framework, combined with a flagrant lack of enforcement of the rules and widespread corruption. Ministries enjoy considerable freedom to recruit their own staff and seek extra remuneration for their employees from projects and other sources. The only constraints are an overall cap on numbers (central approval of the *formasi* and controls over the total wage-bill) and the obligation to seek approval from the regulatory agencies for certain personnel actions.

The regulatory and management framework is characterized by a traditional rules based culture within a closed career system (for example, automatic advancement through the ranks, promotions and internal appointments based on seniority rather than qualifications or performance, no lateral entry to civil service status). There is little results based management and no link between pay and performance. The management of civil servants has been undermined by rampant abuse of the rules and procedures for personnel actions, as well as by the opaqueness of the remuneration system. Widespread patronage and rent-seeking, combined with little enforcement of sanctions, has seriously undermined the accountability of staff and managers.

Despite the plethora of central agencies, however, the civil service is under-managed in terms of ensuring transparency, accountability and consistency in the management of personnel and in building a performance and results based culture. Nor is there a focal point for public sector reform at a high political level that could address the strategic questions: the role, priority functions, personnel requirements and cost of the state and its optimal organization and management at the central and regional level.

The Transition to Decentralization: Still More Ambiguity. The regulatory environment has become increasingly unclear since the enactment of Law 22/99 and this lack of coherence and clarity has grown even worse with the passage of Law 32/04. The decentralization laws have introduced a high degree of instability into the overall regulatory environment for regional autonomy. Civil service management is suffering from the general confusion about the real purpose and nature of regional autonomy and in particular about the roles and functions of the central agencies, the *sectoral* ministries (whose laws have not been revised in the light of decentralization) and the regional governments. The problem is further compounded by the civil service law (43/99), which assumes the existence of a national civil service and mandates a new Civil Service Commission.

An important omission of Law 32/04 is that it lacks the provision of Law 22/99 whereby the regions were given the explicit right to manage their civil services. The Governor, acting in his role as representative of the central government, and the Ministry of Home Affairs (MoHA), has acquired new responsibilities for overall guidance and management of the regional civil service. These changes have raised serious questions about the regulatory responsibility for the regional civil services and created disquiet among regional governments and donors.

As a result of these developments, the sharing of tasks among central agencies responsible for overseeing regional civil service management, including authority for approving specific personnel actions, has evolved. This shift has altered the rules of the game both among central agencies and in their respective responsibilities vis-à-vis the regions, and the sectors, however, the operational implications are not yet fully clear.

Relations between the various levels of government have also been undermined by the increased responsibilities accorded to MoHA under Law 32/04. Regional governments see these as a serious threat to their autonomy. Although MoHA is increasingly taking on development activities through capacity building and other initiatives, it is still primarily perceived as an organization whose main *raison d'être* is to restrict and control the activities of regional governments and civil society through burdensome rules, procedures and approvals.

An example of the shifting roles of central and regional governments is provided by the recent nationally organized and managed recruitment drive. Regional representatives feel that the exercise was a serious infringement of their rights under the decentralization law and a blatant case of recentralization. Certain regional governments have stated that the procedures stipulated did not meet their own standards of transparency and accountability in recruitment procedures.

The lack of confidence in the regions regarding present arrangements between the center and the regions has deteriorated to the point where a few provinces and districts (cf., Yogyakarta and Jembrana) have simply ignored certain provisions of laws or regulations; in turn it appears that the central agencies have overstepped their mandate in the case of the recent recruitment drive. In these instances, therefore, the ambiguities in the regulatory environment have actually resulted in a stand-off between jurisdictions and a serious principal-agent problem on the ground.

Section B. The Role of *Sectoral* Ministries

Law 22/99 stipulated that so called “obligatory” sectors become the responsibility of local governments, such as, districts and cities; these sectors include health, education and public works

and local government took over the management of about 67% of all public sector employees. Line ministries relinquished in principle the personnel management function and their main role became the establishment of minimum standards, a task they now share with MoHA.

But the law does not define what the specific functions of local government are within these sectors and some local governments interpreted this to mean that they were responsible for all tasks within the sectors. Existing *sectoral* laws --still not amended-- added to the confusion about the functions of local governments.

The *sectoral* ministries are still deeply involved, given the lack of skilled manpower in many districts and a reluctance to give up their traditional duties, in planning and managing regional staff and programs. Therefore the development of *sectoral* objectives, policies, plans and related tasks, such as setting minimum performance standards, manpower planning and preparation of the annual *formasi* exercise, are still done in most cases by the sectoral ministries.

The education sector in particular faces major problems as the central and regional governments grapple with the challenge of decentralization. The key issues (see *Education in Indonesia, Managing the Transition to Decentralization*, World Bank 2004. include the unclear and incomplete assignment of functions among the central and regional governments; the need to reorganize the central ministry so that it can articulate and harmonize policies; and need for basic reforms in the management of teachers. This report describes the latter as the most urgent problem and states "our most critical recommendation is for the establishment of a separate teaching service" that would implement merit and performance based personnel management and continuous professional development.

With the onset of decentralization, the management of all civil service teachers in primary and secondary public and private schools was transferred to district governments (with the exception of *madrassahs*). Yet various anomalies and difficulties persist that restrict the districts' freedom to manage and reform their teaching work-force. The central Ministry of National Education is still recruiting contract teachers and paying them directly; *Madrassah* teachers who are civil servants are still managed by the Ministry of Religious Affairs, not by districts. Transfer procedures under Law 22/99 have discouraged teachers from moving to other districts and this constraint has affected morale; teachers are still subject to a variety of corrupt practices and

routinely pay bribes for appointments, transfers, promotions, and selection for training.

The many problems in teacher work-force management, including especially the lack of mobility since decentralization, have resulted in increased pressures from teachers at the school level and their unions to recentralize the management of teachers. In interviews for this report, several district officials expressed their conviction that the recruitment of teachers would indeed soon be recentralized.

Section C. Regional Reform Efforts

The Context. Multiple efforts have been initiated to encourage reforms at the local level since decentralization was launched. Various donors have contributed to these efforts. The district of Sleman; for example, is receiving support from GTZ/Menpan as a one stop shop; AID for performance budgeting; CLGI for performance enhancement; an ADB capacity building project for staff training; an ADB/MoHA project for capacity building for decentralization; and the World Bank urban sector project.

The rush to provide technical services for improvements in regional management has also driven central government agencies, especially Menpan, LAN and MoHA, to compete for donor support in this growth area. MoHA, for example, has established a new Directorate for Capacity-Building that is intended to coordinate and supervise training.

Characteristics of Regional Reforms. For the purposes of this study, it is useful to divide the reforms into personnel management and organizational and other reforms. Personnel management reforms focus on cross-cutting management functions and procedures that apply to permanent civil servants and contract workers. By other reforms, this study refers to various initiatives meant to enhance the effectiveness and efficiency of service delivery in a particular sector, service or unit. Given the purpose of this paper, the analysis concentrates on the former.

Other Reforms. These include: performance budgeting; one stop public services; productivity improvement measures; monitoring of services by citizens' groups; systems of client complaints and subsequent reforms; e-government initiatives; anti-corruption efforts such as integrity

pacts for procurement; other change management programs; training and capacity-building for technical skills related to a sector or function; improvements to *sectoral* management and planning such as new minimum service standards; and implementation of performance standards for services.

It is too early to assess the impact and sustainability of these service innovations, most of which are recent, but there are good reasons to be skeptical: i) to the extent that these reforms stem largely from the initiatives of a few enlightened and dynamic leaders, it could be argued that their continuation and wide-spread adoptions are highly vulnerable to changes in leadership; and ii) experience elsewhere with similar innovations targeted at enhancing accountability through introducing service innovations generally indicates that improved performance is short lived in the absence of more basic, cross-cutting changes, the availability of core resources to sustain them; the performance of management; a results oriented working culture; and transparent incentives.

Personnel Management and Organizational Reforms. The regions have the right, within the regulatory context of decentralization, to undertake basic reforms in areas where they have the required authority. Moreover the lack of clarity about the legal, functional and operational dimensions of decentralization also permits dynamic regional leaders to test the limits of their authority. To what extent has this happened in the case of personnel management reforms?

It is clear that certain regions have used their authority under Law 22/99 to reform essential functions. In most cases reforms are targeted at areas where the regional governments clearly have the relevant mandate. Personnel and organizational reforms have mostly taken place in:

- recruitment (until the latest round)
- the appointment of existing staff to vacant posts
- training
- organizational changes (following to varying degrees the guidelines of Regulation 8)
- improved job descriptions and performance evaluation
- enforcement of discipline and attendance
- rationalization of extra payments taken from the development budget or from regional revenues

Some of these reforms are strategic in that they are intended to improve staff performance through better management functions and incentives and thereby enhance the accountability of the regional public services. Others, however, are not really reforms at all but rather an attempt to reestablish normal, routine management after years of indifference and neglect (for instance, enforcement of discipline and attendance).

Although these reforms are an important beginning, they are narrow in scope and heavily concentrated on improving certain personnel management tools: job descriptions; performance evaluation; recruitment and appointment processes such as the use of external assessment services; and wide-ranging training for insufficiently skilled regional staff.

The constraints imposed by the centre have prevented reforming regional governments from undertaking more fundamental and comprehensive reforms. Thus Yogyakarta Province was prevented from implementing an accelerated early retirement scheme in order better to match individuals and required skills and others fear that at any time the rules of the game may change to the disadvantage of regional autonomy and undo reforms that may have started.

Local authorities are therefore in a difficult position and expressed particular frustration concerning:

- Their inability to move quickly on “right-sizing” and on acquiring the necessary skills to match their identified needs and to staff their new organization; here BKN was largely to blame for blocking more flexible approaches than those current in the regulations.
- The lack of support for their innovations from the DG of Regional Autonomy in MoHA, which they described as lacking a development focus and being only interested in restricting innovations in order to maintain a tight grip on the regions.
- The high existing level of corruption in personnel transactions and the potential worsening of this problem under the stipulations of articles 129-135 of the new Law.
- The lack of a Gol commitment to reform; there is neither leadership, vision nor a single focal point.

Section D. Conclusion

The first decentralization law has resulted in profound changes, yet before the details were defined and the system really became operationally clear, a second law was passed which will aggravate the uncertainties of regulation and management. The management of staff and enforcement of performance standards continue to be fragmented, subject to corruption and generally inadequate. It is evident from the above that the continuing lack of clarity about the rules of the game continues to undermine accountability for the performance of units, managers and staff.

It is also clear that the regulatory and management environment is not conducive to a centrally driven reform effort. Not only is there no strategic focal point or strategy; Gol has not even begun to adapt staffing and organization at the central level to the exigencies of decentralization.

It remains to be seen whether the regulations for Law 32/04 and forthcoming clarifications concerning the civil service law (43/99), the enactment of a new education law and other measures will indeed bring more coherence and predictability to bear. Meanwhile, those regions that want to reform civil service management in order to improve service delivery will have to persevere in their reform efforts with the help of their national and international partners despite the continuing uncertainty and instability of the regulatory environment.

It would not be an exaggeration to state that the regulatory framework is in a critical state, given the renewed uncertainties generated by Law 32/04 and other recent developments. If indeed the responsibility for managing teachers were recentralized, it would constitute a serious and perhaps fatal blow to decentralization in its present form.

The Way Forward in the Short Term. International experience of successful civil service reforms clearly indicates that certain prerequisite steps are essential before reforms are launched, including, i) political commitment and involvement from the top supported by a strong central technical unit; ii) a clear vision of the role and responsibilities of the public sector; iii) an identification of functions to be carried out at the national and the regional levels; and iv) a transparent and stable legal, regulatory and fiscal framework to guide the management of public

employees and the relationship between the centre and the regions.

It is only when these essential pre-conditions and institutional frameworks are in place that an effective reform effort may be carried out. It is evident that Indonesia does not presently have in place any of the essential pre-conditions for a major centrally driven reform; in particular the country is suffering from a crisis in the legal and regulatory framework for the management of the regional civil services. Until the prevailing uncertainties and anomalies are addressed, there is little point in launching across the board reforms.

Experience also shows that in the absence of broad reforms, locally generated change is possible in a context of decentralized management and increasing local participation in the political process. The experience to date with reforming regions in Indonesia seems to confirm this general finding but it also underlines the serious constraints that local governments face in the current uncertain regulatory environment.

The immediate priority is a political recommitment to the spirit and objectives of decentralization by the new Government, including the stabilization of the regulatory framework and the revision of relevant laws and other legal texts. This implies that the authorities should:

- Take the time necessary to ensure that the implementation of Law 32/2004 addresses the many uncertainties and anomalies that have been identified in the text itself.
- Ensure that regulations concerning the management of the regional civil service are prepared carefully with the involvement of all stakeholders and that a new consensus is reached: i) among the central regulatory agencies; ii) between the latter and the *sectoral* ministries; and iii) between the center as a whole and the regions. This effort should be led by a neutral party such as the State Secretariat or an outside consulting firm.
- Implement functional analyses of central ministries and agencies with a view to rationalizing their size, structure and staffing. Given the sensitive nature of this task, it should be done by international specialists.
- Take advantage of the current anti corruption drive to study options for eliminating rent-

seeking in the management of personnel across the whole range of responsibilities from recruitment to transfer to retirement. One option could be to contract out to a private firm the auditing and approval of such transactions. In this case, MoHA and BKN would no longer have direct responsibility for approving transactions involving individuals.

- Design a strategy to replace redundant skills and build a competent HR base.

CHAPTER 2

CIVIL SERVICE REFORM: REGIONAL PERSPECTIVES

1. WEST NUSA TENGARA (NTB)

Introduction

This chapter introduces the Diagnostic and Roadmap study, as well as several important contextual and substantive considerations that shaped both the Diagnostic and the Roadmap.

The consultant team worked closely with its counterparts in order to understand the core functions being studied and the essential problems.

Contextual Factors

The following contextual factors shaped the process of organizing and producing the study and had a determining influence of the content of the Roadmap.

- Like most local governments in Indonesia, none in NTB has taken the initiative to launch reforms in functional areas within their jurisdictions. Nor have they begun preparatory work related to the forthcoming regulations that will replace PP 08. For example, all local governments expect that they will need to restructure and reduce positions but they have not organized themselves in advance to face these issues.
- The consultant team, therefore, took the initiative to help counterparts to grasp the purpose and nature of potential reforms and to distinguish clearly between areas where they have full authority and those where authority is shared with the central government regulatory bodies. *These factors also explain why the Suggested Reform Program of the Roadmap focuses on reforms in areas where there are few central government regulatory constraints and which these local governments can potentially carry out.*

- The consultant team found little awareness that reforms are determined by externalities such as regional development objectives or poverty reduction; as a result there is also little sense of urgency. Moreover, many senior staff perceive reforms as essentially administrative changes which are mandated by the central government.
- The Indonesian civil service is organized as a closed career system characterized by rules and procedures which have been manipulated and undermined and where accountability is sorely lacking at all levels. Therefore, performance in service delivery has deteriorated and the service remains inward looking. These problems have been well documented in many reports. It is within this context that local governments are being challenged to formulate and implement reforms.
- Reform to organizations and personnel is an especially sensitive topic, particularly as it is assumed that the forthcoming regulations will result in a reduction in the number of structural positions. This change implies a serious loss of allowances and perks for those individuals who lose this status. The study was therefore conducted in a climate of uncertainty that did not encourage active participation by all the counterparts.
- It was difficult to carry out the study because of the short working hours of the Indonesian administration, aggravated by irregular attendance at scheduled meetings and a lack of continuity in attendance that hampered systematic and sustained discussions.
- On occasions the counterparts worked well together, particularly when organized on a functional basis (personnel and organization's revenue and expenditure) during the working group sessions.
- The bulk of the work and recommendations on the Roadmap was accomplished with the help of a small team consisting of the heads of the three Bappedas. They took the lead in commenting on the draft Roadmap and in organizing the final workshop.

Key Considerations

The substantive results of the work were influenced by the following factors:

- During the course of the study, in consultation with the World Bank and counterparts, it was decided that a single roadmap would be produced for the three jurisdictions. To the extent that differences in approach among the jurisdictions are already apparent, these would be noted in the document. Moreover, if a decision were taken to fund the implementation of the roadmap, then a more detailed project proposal and subsequent appraisal would be required.
- Local government managers in general are frustrated with the uncertainties and ambiguities that still prevail within the regulatory environment and that undermine effective and efficient management of personnel and financial resources. A presentation at the first Workshop by the Head of *Bagian Organisasi*, Kota Mataram focused on the lack of clarity, transparency and consistency in the application of central government regulations related to personnel actions, organizational restructuring and budget management. This forthright presentation led to a lively exchange about the present realities of regional autonomy with the representatives of central agencies who were present.
- Most local governments are respectful of the power of the central government and its regulatory agencies and generally follow central government guidelines and instructions in areas where policy is dominated by centrally mandated practices (for example, revenue; remuneration of civil servants, training by central agencies, reorganization guidelines). In addition, local governments are generally unaware that they have the right to implement reforms in areas under their jurisdiction. The Roadmap encourages the governments of NTB to lobby the central government in key areas where lack of reform at the central government level is a serious impediment to local government reforms.
- The Roadmap reforms, therefore, focus largely on functions where the local governments have a clear mandate. The strategy of the Roadmap is to encourage local governments to take the lead in some of these basic reforms and to concentrate on reforms where real progress can be made.

- Given the above, the more radical reforms as exemplified by Yogyakarta and Jembrana are not opportune in NTB.
- Local governments throughout Indonesia have already reorganized once after de-centralization and reduced the number of positions, albeit modestly, without shedding staff. The next stage, based on Law 32/2004, has not been implemented as local governments await the new regulations. Whatever the new regulations may say, the problem of over-staffing urgently needs to be analyzed. Most local governments have not yet done the necessary analysis or identified options. Unless the central government designs a special voluntary departure or early retirement scheme local governments will have great difficulty implementing reforms to organization and personnel. Indeed, local governments may strive to find ways to increase the number of administrative units.
- This problem is essentially a result of a lack of thorough preparation and inadequate sequencing of reform measures by the central government. If it is not addressed, it will result in high level of *de-motivation* and inefficiency and continuing high levels of over-staffing, as well as a climate in which reforms cannot be carried out and any momentum towards meaningful change will stall.

Implementation of the Roadmap

If NTB were to consider implementing the suggested reform program with the assistance of donors, it would be essential to ensure political commitment and appropriate organizational arrangements.

International experience clearly shows that the following pre-requisites are necessary for reforms to be successfully implemented:

- Strong political support and participation at the highest level. It is not sufficient for the top leaders to give their blessing and to express their support from time to time; they must actually be engaged on a regular basis in leading reforms.

- A unit in charge of planning and implementing the reforms should be created and located in the office of the Chief Executive of the relevant jurisdiction. This unit must have line responsibility for implementing the reforms (coordinating mechanisms are to be avoided as they lack authority).
- The unit should be staffed with a full-time reform manager supported by experts in Organization, Personnel and Finance. It should also have access to experts in related areas such as law and change management.
- International technical assistance is essential to provide comparative knowledge and experience.

2. WEST SUMATRA

This chapter was prepared in close co-operation with officials from the governments of the Province of West Sumatra, Kota Solok and *Kabupaten Solok*.

It is important to note that the Terms of Reference for this study focus on reforms to core management systems, instruments and procedures in personnel and organization and in budget management and revenue collection.

The consultant team found that preparations for the joint study were well advanced when they arrived. Local counterpart teams were appointed during the first week of the mission and a launch workshop with the three regional teams was held.

A detailed and tight schedule of consultations was then produced, including: data and information gathering activities; a series of technical meetings to validate the diagnostic and start preparing the road map; three separate workshops to discuss and agree on the reforms for the road map; and a final regional workshop in which all three governments would participate.

Throughout its stay the consultant team worked closely with the counterpart teams appointed by all three local jurisdictions and also held technical discussions with other officials. Each lo-

cal government provided considerable information, explained its local situation in detail and engaged in discussion and debate throughout the period of the study. The level of interest and participation from the senior officials responsible for managing this joint study varied among the jurisdictions, however. Participation in the work and interest in reforms were highest in the Kota and lower in the Province and the *Kabupaten*.

It was decided early on that the level of interest and debate and the quality of the information gathered, as well as the differences among the three jurisdictions in their approach to reforms, justified the preparation of three separate diagnostics and road maps (unlike NTB where a single document was written).

Existing Reforms: An Overview

The degree and depth of reforms vary among the three jurisdictions, as does their interest in and potential for further reforms. These factors also favored the preparation of separate road maps for each government; the road maps indicate where reform activities could be carried out.

The diagnostics indicate *that two categories of reforms* have been undertaken so far:

- i. Reforms in areas where local governments have the legal right to innovate in order to improve upon national policies and instruments; for example, supplementary remuneration; strengthening of personnel procedures like promotion in order to enhance accountability and performance; and improvements to procurement.
- ii. Reforms that were carried out under central government's regulations, in particular those carried out in 2001 in order to accommodate the shift in responsibilities under law 22/99 and those mandated under PP 08 of 2003.

As explained in the findings and analysis section below, this is a crucial distinction in that the regulatory constraints of the central agencies restrict the degree to which local governments may implement reforms. Despite these restrictions, the breadth and depth of local reforms vary considerably throughout Indonesia, as indeed is the case also for these three jurisdictions.

The diagnostic and road map contains detailed information on and recommendations for each jurisdiction, and the major problems encountered by these governments as they attempt to reform are analyzed under Major Findings. A brief summary of the status of reform in each government follows:

Existing Reforms in West-Sumatra

e	Province	Kabupaten	Kota
Performance contracts for echelon II			√
More equitable distribution of incentive payments		√	
Fit and proper test for echelon II and/or III-IV	√	√	√
External Assessment for promotion		√	
Re-organization under PP 08		√	√
<i>Pakta Integritas</i> for transaction with the public and the private sector		√	√
Giro to giro: financial transaction by bank without interference		√	
Performance-based budgeting (<i>Kepmendagri 29/2002</i>)	√	√	√
Participatory planning & budgeting for service delivery		√	√
Strengthened procurement processes (<i>Kepres 80/2003</i>)	√	√	√
<i>Pakta Integritas</i> for procurement		√	√

The Province

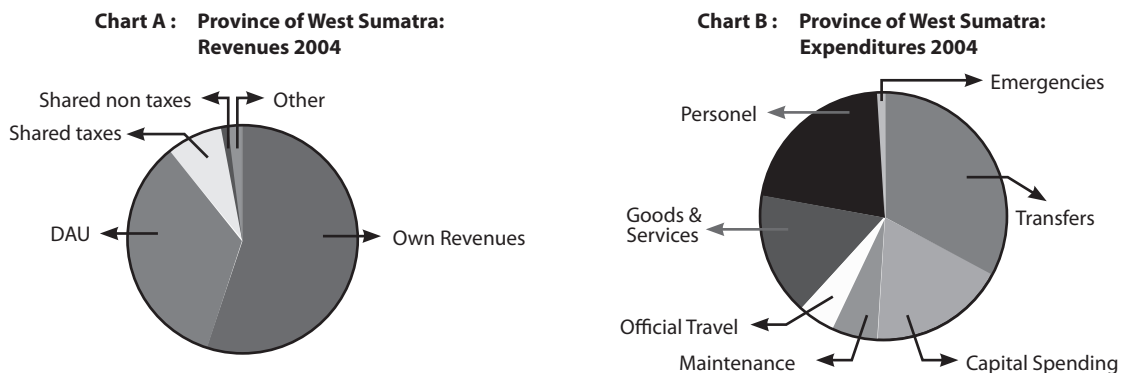
The Province, unlike the *Kabupaten* and the *Kota*, chose not to implement PP 08 but has preferred to wait for the forthcoming regulations for Law 32/04. It froze recruitment in 2001 (it has just restarted for functional positions only) and staff have been reduced by about 4,000 by moving some to *Kabupaten* and *Kota* and by attrition. Overstaffing remains a problem, although its precise nature and magnitude have not been carefully analyzed. Since redundant personnel cannot be retrenched, certain obsolete units have been maintained in order to accommodate

staff; many positions are not staffed with the right skills and no systematic reorganization; for example PP 08, has been undertaken since 2001.

The Province has not attempted, until the recent introduction of the fit and proper test, to reform any of the basic career management processes (see matrix above). Nor has it explored any new ways of analyzing its problems as it awaits the new regulations; indeed it expects to implement the latter using the traditional tools made available by the central agencies (job analysis, etc.) Provincial officials tend to blame the CENTRAL GOVERNMENT for all their problems and do not seem interested in innovations that they themselves could undertake in order to incrementally improve functions under their direct jurisdiction. While they stressed the importance of adhering to regulations, they themselves have not implemented PP 08.

The arrival of the new Governor, the former *Bupati* of *Kabupaten Solok*, is expected to lead to a series of reform initiatives; he has already implemented a “fit and proper test” for echelon positions II-IV that should increase the rigor of promotion decisions.

Turning to financial reforms, the Province of West Sumatra is starting from a relatively strong fiscal position. More than half of its revenues are accounted for by its own sources (see Charts – A and B below);¹ personnel costs are only 1/3 of total expenditure; and the Province has just recorded a sizable surplus (of more than 4% of total spending) in 2004. The main weaknesses are: over-staffing, which is readily acknowledged by senior staff; and delays in budgetary approval, which push much of development spending from the first half of the year into second half (the Province copes by relying upon ‘informal’ local suppliers’ credits).



¹ These data are taken from *Peraturan Daerah Propinsi Sumatera Barat Nomor 4 and Nomor 31 Tahun 2004; Anggaran Pendapatan dan Belanja Daerah Kabupaten Solok Tahun 2005; Statistik Keuangan Daerah Kabupaten Solok Tahun 2004; and Peraturan Walikota Solok Nomor 1 dan Nomor 5 Tahun 2005*

This absence of fiscal pressure appears to have contributed to the slow pace of reforms to date, indeed, almost all reforms have been centrally-driven. In the financial area, the main advances have only been in the introduction of Performance Budgeting following *Kepmendagri 29/2002* and improvements to procurement initiated by *Kepres 80/2003*. In the case of the former, implementation is readily acknowledged to be incomplete with unclear relationships between many budgeted activities and their indicators. Other aspects on performance-based budgeting also fall well short of ideal, resulting, in practical terms, in a budgeting process that is still largely incremental. As for procurement, appreciable progress has been made, but much remains to be done, as indicated in the suggested road map for reform.

Kota Solok

Attendance by managers and staff in the Kota to technical discussions with the consultant team was high and they showed a keen interest in the study. They are well aware of the problems they face in attempting to carry out reforms in the present regulatory context and are frustrated at the failure of the central government to provide them with the policies and instruments they require to carry out the needed reforms. As described in the diagnostic, the Kota implemented PP 08 and found that its prescriptions were not flexible enough for their particular situation. Nor has the use of PP 08 addressed their basic organizational and staffing problems. While over-staffing is not a major issue, some posts are not filled with appropriate staff and there are some vacancies.

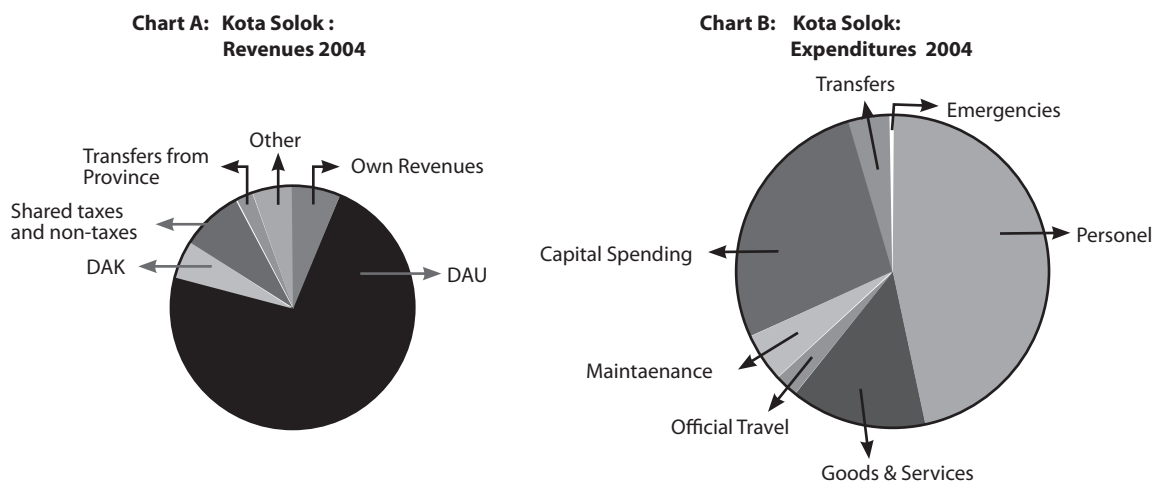
The Kota showed interest in the consultants' explanation of how a functional analysis of its role, functions, organization and staffing needs could equip them to understand their situation and to deal with whatever nationally mandated changes may be forthcoming from the central government.

In the personnel area, the Kota plans to shortly introduce performance contracts for echelon II positions and to later extend this policy to other echelons. It is also studying options for more equitable distribution of income from honoraria based on performance criteria.

Kota Solok's finances are characterized by heavy dependence upon higher levels of government for the great bulk of its revenues (only about seven were locally-generated in 2004; see

Chart A). In discussing this dependence, local authorities indicated that they believe it will be difficult to broaden the local tax base in any significant way.

Given these circumstances, Kota Solok has adopted a cautious approach to managing its finances. Most importantly, the wage bill appears to be under control, being less than half of total spending and only 50-60% of its DAU (see Charts A and B below). In addition, the Walikota believes that further economies are possible in this area, which would give the Kota more flexibility in its spending plans. Another positive aspect of the Kota's accounts is a surprisingly high level of capital spending (27% of spending in 2004; see Chart B).



Like others, Kota Solok has implemented Jakarta-driven reforms in the areas of performance budgeting and procurement. Beyond this, the Kota has made some progress—albeit limited—in the area of participatory planning. More importantly, among the three jurisdictions considered in this study, Kota Solok currently has the most enthusiasm for further reforms; as indicated above, there is considerable room for greater progress, including in the financial area.

Kabupaten Solok

Kabupaten Solok is well known throughout Indonesia for several innovations, including its In-

tegrity Pact, its reform of the basis for paying honoraria and the payment of contractors by deposits directly into bank accounts. These reforms focus on increasing staff morale and thereby performance levels.

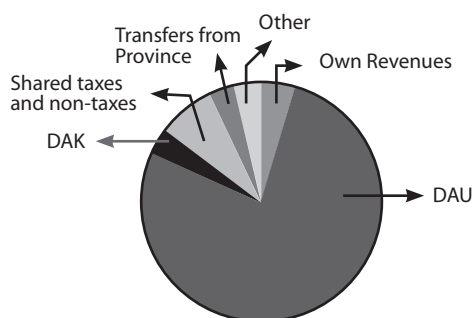
The Integrity Pact is not restricted to procurement procedures and is linked to the reform of the payment of honoraria as described in the diagnostic (see Box 1). It is in return for their pledge to remain “clean and uncorrupt” that civil servants receive these payments. The latter are presently based on attendance and disciplined behavior but it is planned to link them shortly to performance criteria. The present method of paying honoraria in the *Kabupaten* was criticized by officials from the Kota; they found that in providing extra payments to everyone on the basis of attendance, the system was de-motivating for those staff that performed well.

The reforms in the *Kota* and the *Kabupaten* are typical of initiatives that local governments have taken elsewhere in Indonesia to improve accountability and performance. More systemic reforms, such as those focused on the renewal of staffing (retrenchment, early retirement) are not feasible given the constraints of the regulatory context imposed by the central government – see below. As for re-orienting the role and functions of government and subsequent reorganization, it may be useful for reform minded governments to undertake the required analysis on a pilot basis in order to adapt their organizations to the degree permitted or permit them to negotiate later with the central government (see the Road map re *Kota Solok*.)

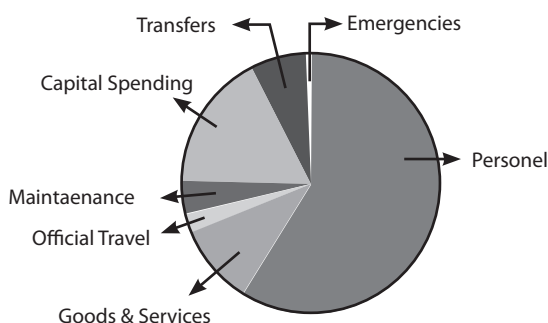
On the financial side, the *Kabupaten* of Solok has a fiscal structure that is marked by extreme dependence upon higher levels of government. For example, in 2004 its own revenues accounted for less than 5% of total revenues (see Charts A and B). In that year, more than 80% of the DAU was absorbed by wages and salaries, and that %age increased significantly in the budget for 2005 to 92%.² Laboring under such a fiscal structure, the *Kabupaten* has little room to maneuver, except by gradually reducing the number of personnel and by increasing local sources of financing. Both have proved difficult to date. As a consequence, capital expenditure is only about 5% of total spending, and it is mainly absorbed by road and infrastructure projects. The expansion of education and health services are financed through the DAK, leaving this *Kabupaten* almost totally dependent upon *de-concentrated* funds to finance better services and to expand services to the poor.

² This is due to unexpected factors associated with the split of the Kabupaten into 2 parts.

**Chart A: Kabupaten Solok :
Revenues 2004**



**Chart B: Kabupaten Solok:
Expenditures 2004**



riven in part by these fiscal pressures, *Kabupaten Solok* has earned a reputation for innovation in its public administration. Like the Province, it has implemented Jakarta-driven reforms in performance budgeting and procurement. But the *Kabupaten* has also gone considerably further in this direction on its own and most of these have financial implications. Of special note in this regard are the introduction of *Giro-to-Giro* payments; the one-door service for payments to suppliers; and the practice of posting fees and days for settlement (see entry No. 18 in the Diagnostics Table). All of these save money by reducing opportunities for corruption.

However, the pace of reforms in the *Kabupaten* has slowed recently, probably due in part to the election of its popular, reformist Bupati as Governor of the Province of West Sumatra. *Kabupaten Solok* needs to re-gain its momentum for reform, as the remaining agenda is long, especially in areas related directly to its finances.

Box 1: Kabupaten Solok's System of Performance Incentives

Kabupaten Solok has a reputation for innovative reforms in its system of public administration. One of these innovations is the *Tunjangan Daerah* (Regional Incentive), which the Kabupaten introduced to better align pay with performance. This Box describes the system's strengths and limitations. In 2004, Kabupaten Solok consolidated local honoraria into a so-called *Tunjangan Daerah* fund. These honoraria had comprised cash payments for various activities, including attendance at meetings,

participation in committees and certain locally-funded projects, in total amounting to approximately 15% of the total wage and salary bill. This amount did not include project-related payments from Jakarta through De-concentrated Funds, which continue to be paid to Dinas staff. It is notable in this regard that the Dinas accounts for more than 80% of Kabupaten staff, the great bulk (70%) being teachers. Payments from this fund are paid in a transparent way, based upon published rates within a simple incentive framework. For 2005, the published rates vary widely from Rp4,500,000 per month for the Bupati to Rp15,000 per month for Assistant Cashiers at schools. Echelon IV officials were close to the median at Rp300,000 to 400,000 per month, while heads of schools ranged from Rp200,000 to 325,000 per month. The incentive framework is attendance-based, with sanctions of 2-4% per day, depending upon the infraction (for example, absence, late arrival or early departure). As of October 2005, a variation of this system was under consideration. It would adopt a scoring system, based upon hours worked relative to officially-mandated work-time (37½ hours per week as of October 2005). The proposed system would pay a 100% bonus (Reward) for those who worked more officially-mandated hours, and apply cuts in the incentive payments (Punishment) from 10-75%, depending upon the number of hours not worked. The system of Punishments allows for further sanctions in the event of repeated (more than 4 per year) large cuts. Both systems introduce a welcome incentive framework for improving office attendance. However, several limitations are also notable. First, the requisite monitoring and reporting systems will be extensive and labor-intensive, which makes enforcement costly. Second, office attendance is only a pre-requisite for improving the quality of public services; better attendance does not address issues of performance, quality of the work and productivity in the office, which ought to be the next step. Third, an attendance-based incentive system becomes increasingly irrelevant at increasingly higher levels of administration. For example, overtime—and working outside the office—is probably a regular part of the job for the higher-Echelon levels and the Bupati's office. The payment for overtime should be abolished and the resulting resources included in the fund. Any other additional payments should ideally be abolished as well. Finally, the proposed Reward-Punishment system looks like it would be under-funded, without a significant reduction to the average bonus. In summary, the Kabupaten's incentive system is a good first start, but it needs to be strengthened by linking these rewards to individual performance. However, the link to individual performance needs to be complemented by the introduction of performance related policies and instruments within the personnel management system.

The Road map: Proposed Reforms

The proposed reforms are targeted at functions where local government's have the legal right to undertake improvements to existing functions and to adapt centrally mandated regulations to local conditions. As prescribed in the TOR for this study, these improvements focus on *basic management systems that are common to all governments* and where capacity is weak: human resource planning; performance management for personnel functions; and performance budgeting.

One possible approach: a set of common activities for all 3 jurisdictions

As may be seen from the three diagnostics and road maps, there are certain proposed reforms that apply to all three jurisdictions and that should be implemented jointly:

- A. Preparations to equip all three jurisdictions to define their positions regarding inter-governmental relations and thereby to lobby more effectively with the central government regulatory agencies; this would also help the local government's to cope with the forthcoming changes to the authority and responsibilities of levels of government in terms of personnel, organization and finance. Such an initiative could include:
 - detailed analysis of interactions with the central government in personnel, finance and revenue areas: where are the major problems in delays (for example, personnel transfers); results of the *formasi* discussions with Menpan; issues regarding reorganization (for example, scoring criteria, flexibility); DAU discussions; and lack of transparency and *multiple-sources* in budget transfers to the Dinas;
 - specific recommendations to the local government; and
 - once the new regulations are out, preparation of a common response.

- B. Development of the basic capacity (by TA and training) for HR forward planning and the development of an HR data-base, the latter should contain sufficient information on personal characteristics and individual careers to permit planning and analysis of personnel to meet projected needs and to adapt to future organizational changes. Above all it would address the most serious common human resource problem faced by local government: the matching of people and jobs.

- C. On financial aspects, certain specific steps could be taken jointly to improve performance budgeting (see the first item in each road map); all jurisdictions need better coordination with the *Dinas* to harmonize programs and reduce overlap in funding from the deconcentrated fund (*dana dekonsentrasi*) and a common training program (in, for example, budget planning, implementation and value for money) would be very useful.
- D. Certain issues related to large revenues could also be undertaken jointly. For example, all jurisdictions have interests in verification of the technical details of the DAU formula. Also, the recommended review of provincial shared revenues encompasses all three jurisdictions.
- E. Virtually all the steps recommended on procurement are best undertaken jointly by all three levels of government.
- F. There are also certain common institutional matters with important financial implications. By way of two examples, the number of financial monitoring agencies needs to be rationalized and the quality of the DPRD upgraded, beginning for instance, with support for finance committees or the parliamentary secretariat.
- G. A common strategy for dealing with international donors would work to the great advantage of all three jurisdictions. This is particularly the case if that strategy were defined by the local governments' needs and not by services on offer from the donor agencies at any given moment.

Activities that could be developed by individual jurisdictions alone or shared with others

Introducing Performance Criteria to Personnel Management

Although the key personnel policies are set for the whole country by the central government, experience throughout Indonesia clearly shows that incremental reforms to improve performance and accountability are still possible within the limits of local discretionary authority. Local examples include: *Kabupaten Solok* has reformed the payment of incentives; *Kota Solok* is pre-

paring to implement performance contracts for echelon II managers and later for all echelon positions; the Governor has imposed a fit and proper test for echelon II-IV level staff in the Province - and for echelon II in the Kota and *Kabupaten*.

Local government could discuss the degree to which joint efforts may be possible in these areas. Policies and instruments that may prove subject to further reforms include:

- improving job descriptions to include the output of tasks
- performance reviews (reforms to complement DP3) to be more focused on outputs and performance
- discipline
- promotion (for example, use of external assessment);
- the treatment of honoraria/incentives (see Box 1)
- enhancement of accountability for attendance and work (introduce a performance orientation in order to enhance individual accountability)
- measures to improve transparency and honesty in the management of funds (cf., *pacta integritas*; special incentives for revenue staff)
- training: options for organizing and funding training locally based on actual needs

As specifically concerns financial issues in this regard:

- a review to broaden the local tax base could be done separately or jointly by the *Kabupaten* and the Kota (this is not an important issue for the Province at present)
- some jurisdictions (for example, the Province and the Kota) need to adapt the innovations of other jurisdiction (for instance, the *Kabupaten's* system of performance incentives)

Separate activities:

- Certain reviews of processes—that are significantly different in their details between the different jurisdictions—are best done separately; for example, an initiative to identify bottlenecks in the Budget preparation process to introduce a more realistic schedule; to add more discipline to meet that schedule; and to reduce the need for supplementary budgets
- The Province (which has a mandate for monitoring lower level governments) needs to act on its own, to introduce time-lapse-based reviews to speed-up processes like

- budgetary oversight.
- The Kota expressed interest in undertaking, on a pilot basis, a fundamental review of its role, functions, organization and staffing in order to permit it to meet its targets better and to be in a stronger position to negotiate with Jakarta over the *formasi* and other issues. On the budget side, issues to be addressed include; prioritization and reallocation of expenditures; the linkages between priorities, planning, budgeting and activity implementation; and broadening the local tax and “*retribusi*” base. Such a review would also give this government a grasp of modern analytical tools that may be used to supplement the instruments mandated by regulations emanating from the central government.

Analysis

This section attempts to summarize the major issues relevant for reforms at both the regional and central levels (in organization and personnel and in expenditure and revenue). It is based on the diagnostics that underpin the West Sumatra regional road maps, as well as on studies of the central government and its regulatory context.

It is obvious from the evidence of the diagnostics and road maps for West Sumatra that, in the medium term, *effective decentralization depends crucially on reforms at the central government level* in order to bring stability, coherence and predictability to the regulation and supervision of the regions.

The lack of clarity in the regulatory framework for managing decentralized budgets and personnel, documented elsewhere, emerges as a major constraint to the implementation of regional reforms.³ The small number and narrow range of locally generated reforms carried out in West Sumatra reflects the very restrictive nature of regional autonomy: local government enjoy little discretion in the planning and management of their budgets and staff; and most have no financial independence as they are caught in an intricate web of regulations, approvals and pressures from the regulatory agencies and the *sectoral ministries*. Often they receive contradictory signals from the Center. For example, regional governments are required to have a maximum of 12 Dinas under PP 08, yet certain sectoral ministries continue to insist that each

ministry, if it is to support programs to the regions, requires a single --and not a combined-- Dinas as its counterpart at regional level.

Law 32/04 has undermined the spirit of law 22/99 and strengthened the powers of the central government over the regions, for example, recruitment has been largely recentralized; and the regulatory role of MoHA has been strengthened. Transaction costs have gone up as the number of approvals required by the central government has increased. More transactions also mean additional administrative delays and more opportunities for corruption in the central-regional relationship, as central agencies may demand informal fees for what should be routine transactions.

Box 2: The situation of the Dinas at the local government level after decentralization

Since implementation of decentralization in 2001, the *Dinas* in the Province, *Kabupaten* and Kota have acquired responsibility for delivering services to the people. This box describes the problems that have arisen among various local governments, as well as between local governments and the central government, as the Dinas attempt to provide public services in an efficient and effective manner. These problems have resulted in overlapping and a duplication of activities and their related funding; a lack of transparency and coordination; inadequate flows of information; unclear lines of responsibility; and consequent inefficient and ineffective service delivery by central governments.

The current situation appears to stem from i) the central governments regulatory, policy, and operational interventions, and ii) local governments own behavior which at times exploits the lack of clarity and duplication in the central governments role to their own advantage.

- i. Regulation PP 08/01 was intended to assist local governments to streamline their organization. It appears, however, that this regulation places restrictions on local governments that prevent them from reorganizing to meet local needs in an efficient and flexible way. In particular the PP imposes a rigid method and criteria, including a scoring system that determines the number of *Dinas*, *Badan* and *Kantor* for local governments. This method has also been disruptive in that local governments need, as a consequence of restructuring, to deal with overstaffing without adequate policies for redundancy. Some local governments have not implemented PP 08 and

³ See Civil Service Reforms at the Regional Level: Opportunities and Constraints, World Bank, 2005 by Steedman and Kenward.

have maintained existing units, whose responsibilities have already been transferred to other local governments, simply to provide jobs for potentially redundant staff.

In addition, *sectoral* Ministries are attempting to force local governments to create a single local representation at *Dinas* level. This policy contradicts the existing regulation PP 08 which restricts the number of *Dinas* at local government level and may not be relevant to local needs. Why should a local government have a fishery or a mining *Dinas* if this sector is irrelevant for the region?

- ii. The role of de-concentrated programs further complicates the management of *Dinas* budgets and resources and creates perverse incentives for local governments to exploit the uncertainty surrounding their role and that of the central government.

Deconcentrated resources provided by the central government for local services are unpredictable, late and undermine local planning. In addition, some central programs are managed through the Province with the help of the *Kabupaten* and *Kota* and some are managed directly by the *Kabupaten* or the *Kota*. This has led to confusion about the precise roles and responsibilities of the two levels of local government. For example, a *Dinas* may hide from the local government the existence of funds received for the management of central government programs in order to maximize its own resources. This lack of transparency results in duplication of activities among *Dinas* and prevents local governments from planning and managing development programs in a coherent and efficient way. Training, for example, may be planned and carried out for the same target group by two different *Dinas*. Teacher training may be conducted by a Province as well as by a *Kabupaten* or *Kota*.

Conclusion: inefficiencies in the *Dinas* stem from broader systemic problems, in particular the central governments apparent reluctance to clarify in sufficient detail the rules of the game for decentralization, as well as the incomplete nature of the reforms already launched.

The reforms carried out by regional governments in West Sumatra have been restricted to areas where local governments enjoy some authority to innovate and/or have been carried out under central government regulations such as PP 08. Unfortunately these regulations have

proved inadequate and remain incomplete and as a result local government in West Sumatra and elsewhere have not been empowered to carry the reforms they have launched to their logical conclusion based on local needs. The reforms remain partial since certain key elements are missing; in particular, the lack of an early retirement scheme for redundant staff means those local governments do not have a free hand to reorganize effectively and to appoint “the right person in the right job.”

Box 3: Excerpt from the Kota Solok diagnostic

The instability of the legal environment has caused slow and incomplete restructuring of the organization. At present the Kota is waiting for the new regulation based on Law 32/04. Organization reform is presently at a standstill and an evaluation of the last restructuring is ongoing.

The result of the implementation of the Decentralization Law is overstaffing on the one hand and an increase of the workload and a lack of technical skills on the other hand.

The motto of the Kota is still: “rich in function, poor in structure”.

The implementation of PP 84/00 has not resulted in a more efficient organization.

Management of the regional civil services is seriously undermined by the inadequacy and obsolescence of many of the policies and instruments of the central civil service management system that regional governments are obliged to apply. The central government has failed to reform the basic policies and instruments of personnel management, many of which are obsolete, weak and inappropriate for a coherent transition to real regional autonomy (for example, job analysis⁴, DP3, the pay and grading system). In fact all the basic functions need to be reviewed and/or simply replaced, including: the remuneration and grading system (the distinction between structural and functional jobs has created rigidities and perverse incentives that seriously hamper the effective management of personnel and impedes the development of professional skills and attitudes); job analysis; performance evaluation; the credit point system for functional positions.

³ An unpublished World Bank report from 1993, Indonesia-Civil Service Issues, identified several major weaknesses in using job analysis to produce job descriptions and for broader purposes like mapping the functions of work units in order to reduce the bureaucracy. The report questions whether the use of job analysis should be continued in the absence of more fundamental analyses focused on determining the appropriate size, cost, role and functions of the civil service.

In the financial management area, however, the central government is attempting to introduce more modern systems and methods such as Performance Based Budgeting. However, these systems will need to be made compatible with those in Organization and Personnel once the latter are reformed.

The reforms in Organization and Personnel are stalled and there is no indication from the central government that it will move in the forthcoming regulations to equip itself and local government with the resources, regulations and procedures required to complete the reforms in a coherent and consistent fashion. For a description of the priority actions that the central government needs to take to permit coherent organization and personnel reforms to be completed, see **Annex 1**.

Turning to finances, local governments are beset by many well-known, deeply entrenched problems. Most importantly, they lack the requisite financial independence to address their legitimate local needs effectively. This arises because most local governments are heavily dependent upon higher levels of government for revenue; the local tax base is narrow; and in many cases critical tax parameters are controlled by the Center. On the expenditure side, a rigid wages and salaries bill generally accounts for the great bulk of spending; over-staffing is widely acknowledged as a sizable problem; there is costly duplication of some services due to vague, overlapping institutional mandates; and capital spending is often low. In addition, the large revenue items (especially the DAU) are highly vulnerable to political intervention, and many other types of taxes are subject to collection fees of one form or another.

Conclusion and Recommendations

No Significant Change is Coming from the Center. Unfortunately, none of these problems appear likely to be resolved any time soon. Indeed, there are indications that centrally driven policies are still moving in the wrong direction. In the meantime, local governments will have to live with this unsatisfactory situation, using whatever flexibility they have to improve their circumstances in areas under their jurisdiction. The analysis of this study indicates that there are no simple, broad-based solutions to address the many problems. Rather, this study has uncovered a surprising number of small steps that reformist local governments could take on their own

initiative, that is, without awaiting direction or approval from Jakarta.

Certain Local Solutions are Feasible. The various steps vary somewhat by jurisdiction, reflecting their current taste for reform and, perhaps, the phase of the political cycle. For the jurisdictions studied here, the Province is still resistant to significant change; the *Kabupaten* looks to have lost some of its previous momentum for reform, at least for the time being; and the Kota seems to be gaining momentum rapidly. But looking past this complication, the various steps may be conveniently grouped as described below (see the road map for details).

This study concludes that the best approach is to emphasize the following priorities (see road map):

A. Securing sufficient financial independence for local governments to make progress in meeting legitimate local needs:

- Encourage local governments to reorganize according to their needs and introduce more performance management policies and tools;
- Increase Own Revenues, by broadening the tax base, restructuring some tariffs, and managing certain assets for greater financial return;
- Manage Expenditures Better, including by efforts undertaken jointly by all three jurisdictions to reduce over-staffing; reduce overlapping in funding and programs; and eliminate spending that violates principals of transparency and accountability;
- Lobby more effectively with the Center, including through regional and national associations and the international community;
- Introduce rigorous methods to streamline the organizations; and
- Manage their human resources through the introduction of forward planning and performance based instruments.

In order to achieve these priorities, the local governments of West Sumatra need to define consistent and coherent reform programs and sequence these reforms carefully. In addition, the central governments should manage the technical assistance offered in a coherent way based on their own needs and not on the preferences of individual donors.

3. METHODOLOGY USED

Questions were prepared for discussions with representatives of local governments. These were prepared as open questions in order to ascertain the nature of real practice within these jurisdictions. The methodology was used to prepare the diagnostic, road map and reform options. For an example of the diagnostic, road map and reform options see Annex 5.

A. Budget Planning, Policy Formulation, Execution and Monitoring

1. What types of budgets do you use? (for example, line item budgets, performance budgets). Are they linked to program objectives and performance indicators? If yes, how do you actually link the budget to performance?
2. How do you monitor and evaluate budget performance?
3. Are you doing an adequate job in developing expenditure plans?
4. Do you have sufficient time to prepare, execute and monitor budget performance?
5. Can you avoid overlap in the budget? How?
6. What role does the DPRD (regional parliament) play in budget policy formulation and approval?
7. How does the central government inform local governments that their programs and budgets have been approved?
8. What percentage of your DAU represents cost transfers exclusively for the wage bill?
9. Do you consider de-concentrated funds in your planning? How?
10. Are *Kabupaten/Kotas* involved in the provincial budget planning?

For *Kabupaten/Kota*:

11. Do you factor the provincial budget into your plan? How?
12. How often do the local governments prepare and approve a supplementary budget?
13. Is there any compliance, performance or financial audits ever conducted?

B. Procurement

1. How does the procurement system operate?
2. Do procurement and tender committees use preferred vendor lists and are vendors

- required or encouraged to register with any local government?
3. Does your service or bureau ever purchase goods and supplies in bulk or purchase items in conjunction with other services or bureaus?
 4. How do you notify the public and disseminate information about procurement opportunities?
 5. Do you employ Integrity Pacts to bolster transparency and prevent corrupt procurement practices?
 6. What policies and procedures are used to resolve conflicts in bidding or procurement (for example, complaints against a winning bidder, non-compliance of a bidder, a vendor who fails to provide goods or services as described in the contract or has failed to meet any other contractual obligations with regard to quality and control issues)?
 7. What channel(s) exist for a vendor to file a complaint if they believe any aspect of procurement processes and procedures have not been transparent or fair?

C. Revenue Planning, Policy Formulation and Generation

1. What are the sources of tax revenue and non-tax revenue?
2. What are your most productive local taxes and user fees?
3. Which taxes are collected by the central government and shared with local government?
4. Do you have a revenue generation plan?
5. How is the tax collection fees distributed?
6. Did you meet your revenue targets for the 2004 Fiscal Year?
7. When was the last time taxes and fees were increased?
8. What happens if revenue collected exceeds the projected local revenue budget?
9. Which taxes are shared with the Kabupaten/Kota and how are they distributed?

D. Organization Structure

1. How was the organization structure changed in response to the implementation of the decentralization Law 22/99 and to PP 08/03?
2. Were any changes made to streamline the organization?

- Number of working units
 - Number and functions of positions
3. How has the potential reduction of the amount of structural positions been addressed? Describe options for solutions!
 4. What efforts need to be made to address the problem expected to occur in transferring staff from structural positions to functional positions?
 5. How has overlap in tasks and functions been addressed? For example, between Setda and Dinas. Describe options for solutions!
 6. Are there any on-going preparations to implement recommendations of the study in light of the forthcoming Government Regulation which will replace PP 08?
 7. What arrangements have been planned to facilitate the implementation of streamlining the organization?
 8. Is there technical capacity available; is it responsible, what is the time frame, etc?

E. Personnel

a. General:

Number of staffing positions and employees in relation to development objectives and actual functions

- Age profile
- Education level of position holders in relation to the job requirements of structural positions
- Gender

b. Contract staff (non teachers)

- Number
- Functions
- Relative importance of this group

c. Job Analysis

1. Has job analysis been done?
2. If so, what method was used?
3. Is the quality of the job analysis adequate?

4. Has the job analysis yielded good job specifications and descriptions?

d. The right person in the right job

1. Discuss, for example:
 - Overstaffing at certain levels
 - Mismatch of qualifications (background, skills) with the requirements of the job description
2. What kind of solutions?
 - Early retirement
 - Re-training
 - Re-deployment
 - Management development
 - Attrition

e. Remuneration and other incentives

1. Are extra emoluments, benefits or other advantages provided to all staff in a transparent and equitable way?
2. Is this practice linked to an enhanced performance and accountability system?
3. What are the sources of such payments (for example, development budget, local revenues)?
4. Have regional governments attempted to enhance accountability and performance of managers and staff?

f. Enforcement of discipline and attendance

How are discipline and attendance enforced?

g. Human Resource Planning

1. Is there any HR Planning?
2. What does it consist of?
3. Are any institutions consulted to avoid overlap?

4. Is there 3-5 year planning and which instruments and criteria are used?
5. How is the transfer from structural positions to functional positions addressed?
6. Do they take into account potential overlap with institutions working in the same technical or service functions due to new regulations?
7. How is the transfer planned and what provisions can be made to smooth the process?

h. Recruitment

1. Who determines the rules and regulations?
2. What specific criteria?
3. Explain the nature of the exam/competition

i. Promotion, advancement and Transfer

1. How is a person assessed for promotion?
2. Who's responsible?
3. What criteria?
4. Who does that?
5. What are the regulations regarding promotions progress through the ranks?
6. Describe the procedures for transferring within and outside Kabupaten, Kota and the Province
7. Describe impediments to transferring staff to other jurisdictions

j. Training and Development

Training policy for staff:

1. Are there training needs analyses?
2. What are the types of programs for different levels and categories of personnel and what are the criteria?
3. Criteria for national or international training?
4. What training is compulsory and relevant for career development?
5. Are there job-related training plans and are they ever offered by local government?

k. Performance Appraisal

1. Describe the theory and practice of performance appraisal
2. Does the PA system have any impact on accountability of managers and staff and on unit performance?

l. Management of Work

How is the work defined?

1. What does work consist of?
2. Are tasks identified?
3. Are these tasks written down?

How is the work organized?

1. How is the work done? By teams, individually, or in working sessions?
2. What are the preparations for meetings, for example, minutes, agenda, etc.?
3. Routine versus exceptional work?
4. Are there work schedules?

How is the work assigned?

1. Is the workload defined and is it in writing?
2. Are the roles and responsibilities clearly defined among all the parties?
3. How is the workload communicated?
4. Are there any deadlines?

How is the work managed?

1. Is there regular exchange and update on the progress made between managers and employees?
2. How is the person doing the work held accountable?
3. Is the final result of the work discussed and approved by the manager?
4. How is the attendance of employees enforced in relation to the work to be done?

4. PROPOSED PILOT IN KOTA SOLOK, WEST SUMATRA

Rational and purpose for the proposed pilot

During the preparation of the Diagnostics and Roadmap, *Kota Solok* showed the most enthusiasm for further reforms among the six jurisdictions (three in West Sumatra and three in NTB) that participated in the study. *Kota Solok* expressed keen interest in a pilot. The *Walkout* and his staff are well aware of the problems they face in attempting to carry out reforms in the present regulatory context and are frustrated at the failure of the central government to provide them with the policies and instruments they require to carry out the needed reforms.

The *Kota* expressed interest in undertaking, on a pilot basis, a fundamental review of its role, functions, organization and staffing in order to permit it to meet its targets better and to be in a stronger position to negotiate with Jakarta over the '*formasi*' and other issues. On the budget side, issues that would be addressed include; prioritization and reallocation of expenditures; the linkages between priorities, planning, budgeting and activity implementation; and broadening the local tax and *retribusi* base. Such a review would also give this government a grasp of modern analytical tools that may be used to supplement the instruments mandated by regulations emanating from the central government.

The draft Terms of Reference for TA for the pilot, costing, a timetable and other relevant preparatory documents have been prepared. The ToR describes the cross-cutting substantive issues to be addressed and stipulates the general objective, the content of the pilot and the TA required for the five key areas as discussed above: i) the right person in the right job; ii) a transparent and equitable remuneration package for all; iii) performance management for all; iv) sound local own revenue (PAD) management; and v) Redesigning/Improving Local Financial Administration. In addition, TA for the management of the project and for facilitating negotiations with the central government is included. The *Walkout* will need to undertake discussions with the province and the central government concerning the reforms to be piloted. The ToR includes provisions for TA to facilitate the negotiation of an agreement.

For a complete description of the proposed pilot, including Terms of Reference and other related documents, please see report 2: Innovation in the regions: A new initiative for Kota Solok.

CHAPTER 3

FINANCIAL ISSUES IN CIVIL SERVICE REFORM

This part examines financial aspects of civil service reform, emphasizing opportunities, constraints and options over various time horizons. The focus is on scenarios that provide rough estimates of the (net) cost—and affordability—of broad-based, conventional reforms at the regional and national levels of government. Where such reforms are not affordable, this study suggests low-cost options and provides suggestions for priority areas of reform. On related topics, this paper revisits the issue of whether Indonesian civil servants are underpaid; investigates the reliability of the recent census of the civil service; and looks at specific *kabupatens* for evidence on cost, affordability and lessons to be learned in local reforms.

How Much Over-Staffing?

It is taken for granted in this analysis that the Indonesian civil service is generally over-staffed, although there are important issues of composition among sectors. Consequently, the main issue is the extent of general over-staffing. Fully addressing this issue would entail a major ‘needs assessment’ that is well beyond the scope of this study. Instead, new evidence is examined from two main sources:ⁱ a detailed ‘needs assessment’ of the Jakarta Commercial Court; and experience in the field. On the basis of existing workloads, the former suggests a major down-sizing, of approximately two-thirds. As for the second source, DKI Jakarta sought the same magnitude of right-sizing, 70% by 2007. Kabupaten Jembrana is reducing its civil service by much less, about 10% by 2006. By contrast, Bulukumba has been trying to increase its civil service by almost 8%.

This paper does not take a firm position on the desired magnitude of civil service right-sizing. However, considering the evidence noted above—and the strong case that can be made for exempting certain groups, like teachers—this paper considers an illustrative 10% cut, which looks like it would be a strong start in right-sizing Indonesia’s civil service.

Evidence on Pay & Reform: Are Indonesian Civil Servants Underpaid? The issue of the adequacy of pay for Indonesian civil servants has become controversial within the World Bank since the financial crisis of 97/98. Further examination of the issue was included in this consultancy's ToRs. To make further progress,ⁱⁱ this paper assembles key pieces of evidence and proposes a policy position for future thinking on the issue.

Evidence from Sakernas. Indonesia's labor force survey, Sierras, provides comparative data on earnings by industry. These data indicate that average government wages have increased rapidly during the past 3 years, at rates well above sectors that are dominated by private activity. By 2003, wages of government employees were much higher than in major sectors dominated by private activity.

Other New Evidence. Three other pieces of evidence are notable in this context.

1. There is very little non-retirement turnover in the Indonesian civil service, indicating that government workers are not dissatisfied with their work situation, despite claims of low wages.
2. Major excess demand exists for entry-level civil service jobs at current wage rates, and contract employees are willing to accept wage rates well below civil servants' rates to position themselves for preferential access to the civil service.
3. Job applicants have been willing to pay (i.e., bribe officials) to be chosen for civil service jobs.

Consistency in the Variation. There is a striking consistency in accumulated evidence on the adequacy of civil service pay. Namely, job-to-job comparisons indicate that Indonesian civil servants are seriously underpaid, but person-to-person comparisons indicate that average salaries of Indonesian government employees are substantially above those in the private sector. This suggests a methodological weakness with the job-to-job comparison, namely that truly comparable jobs are often difficult to find. In developing countries, 'comparable' jobs are almost always found in formal sector enterprises, but these are normally only an option for the elite of the civil service. Tracer studies indicate that for the great bulk of separated public sector employees, the relevant alternative is the informal sector (including agriculture) which is paid

much less than the civil service in Indonesia.

Job-to-job comparisons clearly indicate that quality civil service managers (and some staff with highly marketable skills) are underpaid. However, it would be a costly mistake to generalize this result to the average civil servant, and to use pay policy as the primary instrument to close the gap. The trick is to link the requisite, large pay increases for select groups to performance, which appear to be very difficult in the current institutional environment.

And a Further Word on Corruption. Certain groups within the civil service are entitled to so-called functional allowances that can be a significant component of overall salaries. Among these groups are Attorneys and Tax and Customs officials who are widely considered to be the most corrupt of Indonesian civil servants. Clearly, the current level of the functional allowance has not been an effective deterrent to corruption within these groups. This casts further doubt upon pay policy as a primary instrument for reducing corruption within the Indonesian civil service.

The Civil Service Census of 2003

A key piece of data for this study is the 2003 census of Indonesia's civil service. Unfortunately, there are lingering doubts about its reliability,ⁱⁱⁱ and more is needed by way of quality assurance. For example, the census data should be checked in detail against Ministry of Finance payroll information. Also, a sample audit should be undertaken. If anything more than a minor error rate is discovered, the census should be repeated with much tighter controls. Furthermore, on-going follow-up (perhaps on a rotating, regional basis) would go a long way towards ensuring the continuing quality of these data.

Results of the Financial Scenarios

As summarized below, this study examines the (net) costs of four^{iv} civil service reform scenarios, measured in relation to a very neutral baseline projection.^v All scenarios include an estimate of the budgetary impact of civil service pensions. In considering these scenarios, a key point

should be noted, namely that across-the-board right-sizing disguises an important effect on the center-regional breakdown of fiscal costs. In particular, if the cuts are not across-the-board, certain institutional arrangements built into the present system of block grants to regions (the DAU) are a significant disincentive for *kabupatens* to undertake right-sizing on their own (see Box 4 of the main report).

Scenario #1: Aggressive, Across-the-Board Right-Sizing, Financed Up-Front. This reform scenario entails a once-only, 10% cut in the size of the civil service with a modest retrenchment package. The cost of the compensation package would be shared by center and regions in proportion to benefits.

The estimated up-front cost of this right-sizing is some Rp17.75 trillion (almost US\$2 billion at current exchange rates), of which only about half is recovered during the first year of reform. Regions bear the bulk of the costs, indicative of the current distribution of numbers of civil servants. Beginning in the second year of reform, net financial savings (relative to the baseline projection) accrue at the rate of almost 0.4% of GDP per annum. Consequently, the cost of this right-sizing is fully recovered by early in the third year of the reform.

Implementing this Scenario would probably be difficult, partly because the up-front costs are large. Also, it's difficult to imagine how a coordinated, across-the-board cut could be implemented under Indonesia's current institutional arrangements unless it were fully financed and executed by the center. At the center the only source of financing of this magnitude is a cut in fuel subsidies, which has proven difficult to date. Furthermore, it seems unlikely that the savings from such a cut would be spent on civil service reform.

Scenario #2: Aggressive, Across-the-Board Right-Sizing, Financed Over Five Years. This scenario is exactly the same as Scenario #1, but the settlement package is paid out in accordance with Government Regulation PP 32/79.^{vi} From the government's side, this Scenario is very attractive, largely because the government saves money immediately (more than 0.1% of GDP). By the sixth year, these savings build up to almost 0.4% of GDP. This Scenario is less attractive for the employees, because it requires that retrenched civil servants give up all allowances for five years without compensation. Almost certainly the government would have to provide some sweetener to make this a voluntary right-sizing (see Section V, below).

Scenario #3: Net Hiring Freeze. Under this scenario, the size of the civil service would be held constant for five years, which permits gross hiring of about 110,000 per year to replace staff who leave the civil service for one reason or another. The financial savings cumulate slowly, at less than 0.1% of GDP per year. After five years of this reform policy, the savings total about 0.3% of GDP per annum. Effectively, this scenario is a return to the policy of the past decade, known as 'zero growth'. Its sustainability largely depends upon the capacity of the authorities to direct the new hires into priority areas. Current institutional arrangements are not encouraging in this regard.

Scenario #4: Interim Damage Control. The final scenario presumes that downsizing in any form is too difficult to implement. Instead, the authorities adopt a strategy of containing the size of the problem until more momentum for reform develops.^{vii} The gains from this strategy are only moderate on an annual basis, but they cumulate quickly, if they can be sustained for a decade. By then, total savings are more than 0.75 of 1% of GDP per annum, the largest of any of the options considered above. As in Scenario #3, the sustainability of this option depends upon the capacity of the authorities to direct the new hires (of about 150,000 per annum) into high priority areas.

Low-Cost Options & Priorities

If right-sizing proves too difficult or expensive, there are other options that a reformist regional (or central) government could pursue, as discussed below.

Contracting. This is a very useful approach that is already proving popular in the regions. The financial advantages are:

- It's cheap. Contract workers are willing to accept wages well below (roughly 1/3) those of a regular civil servant, because the regular civil service is overpaid at lower levels.
- It provides flexibility to adapt wages to local labor conditions, instead of being centrally-determined by the national government.
- The government's commitment is time-bound by the length of the contract.

- Separation is easier because it can be made explicit in the contract.
- There are no hidden long-term liabilities, like pensions.

Extended Leave With Pay. The simplest way to shed an unwanted employee is to put him/her on extended leave. This costs the government nothing and may actually save money by reducing a few allowances (like meeting attendance and transportation); on a large scale, it would save on office space, maintenance and electricity.

Extended Leave as a Sweetener. If extended leave is perceived as unfair (because it is interpreted as a reward for poor performance), the right to extended leave could be granted as part of a retrenchment package.

Suggested Priority Areas. Governments will have their own ideas about priority areas for reform, reflecting local preferences and past neglects. However, from a financial perspective, priorities should emphasize processes like better cash management; reforms in areas that are self-financing, like better contracting and costing procedures; and charging for services that legitimately justify user fees (retribusi). Lessons from the field also point to the importance of building up local financial independence, in one way or another. The experience of Bulukumba indicates the difficulties of improving local services that need the center's approval to hire more civil servants. By contrast, Jemberana and Yogyakarta have forged ahead on their own, right-sizing their civil service through attrition and using the savings to hire low-cost contract workers.

Policy Conclusions

Suggested Position on Pay Policy. There is very little doubt that the great bulk of civil servants in Indonesia are poorly paid, but this mainly reflects average income levels in the country. Indonesia's enormous supply of unskilled labor covets even low-paying, sub-entry-level jobs in the civil service. By contrast, upper levels of the civil service (and groups with highly marketable skills) appear to be seriously underpaid. Overall, the evidence indicates that the great majority of Indonesian civil servants are still better off than if they were to move into the domestic private sector.

The wider problems of Indonesia's civil service are over-staffing, low productivity and a salary policy that separates pay increases from performance. These factors combined with wide opportunities for corrupt behavior—and no negative consequences for pursuing them—produce Indonesia's civil service of today.

Large salary increases are not a stand-alone answer to this problem. Unless pay increases are tightly linked to performance through major changes in management policy, increases in salaries will just be a windfall gain for the average civil servant. There will be no visible change in the quality of the public service; it will only become more costly.

Suggested Position on Wider Civil Service Reform. Estimates exist of the cost of simultaneously addressing the problem of low pay, low productivity and corruption. But the best recent estimates are way out of line with affordability, and there are serious doubts about their implement-ability. Better near-term financial policies should emphasize:

- Low-cost options to reduce the size of the civil service, most notably extended leave with pay.
- A program to reduce the size of the civil service through attrition, replacing them with contract employees who are placed in jobs of high priority to local governments.
- Reform of the DAU to eliminate impediments to unilateral civil service reform by the regions.
- Pressing ahead with consolidated budgeting to improve the transparency of pay policy by moving all special allowances from the development budget into the routine budget.

The scenarios examined in this study point to a different approach over the medium-term. To summarize:

- Any across-the-board right-sizing (of even 10%) appears difficult in current circumstances. Either the up-front costs are too high, or current institutional arrangements are too complicated.
- A right-sizing by a net hiring freeze appears possible. It allows new hiring of some 110,000 per year and many more, if they are contract employees.
- Sustainability of a net hiring freeze depends critically upon the government's capacity to direct new hires into priority areas.

There is a serious risk that none of these policies will be implemented any time soon. Accordingly, until more momentum for reform can take root, the interim strategy should focus on policies to contain the extent of the problem. The main instruments in this regard are:

- Budgetary policy that resists pressures for appreciable real increases in civil servants' salaries.
- Employment policy that resists pressures to increase numbers of civil servants in any significant way.
- Employment policy that directs new hires into high priority areas, through contracting wherever possible.

CHAPTER 4

POSSIBLE FOCUS AND ORGANIZATION OF CENTRALLY DRIVEN REFORM INITIATIVES

Introduction

The purpose of this chapter is to present ‘*An assessment of the likelihood that the Gol will undertake a centrally driven reform initiative and the identification of its possible focus and organization.*’

It has become apparent in recent months that renewed interest in a centrally driven reform initiative has developed:

- Many of the principal actors in the Gol and the donor community have prepared studies and/or plans focused on civil service reform at the central level (see Annex 1-4 regarding the various Gol proposals) The World Bank, the Partnership, the KPK, the Asian Development Bank and other donors have been encouraging the President to set up a task force to manage the central civil service reform effort and have provided his office with documents on the institutional and strategic dimensions of reform.
- An ADB document, written in collaboration with the World Bank and the Partnership, has been issued; *The President’s Governance Reform Initiative*.
- “From Planning to Action” outlines the key factors and makes detailed recommendations on aspects such as stakeholder participation and the staffing and organization of the proposed secretariat.
- Relevant legal documents are being prepared or updated, including the Civil Service Law 4/99, PP 25/00, and PP 08/03. Some of the latter also concern the regions and their relationship to the central government; in addition, MoHA has published its Grand Strategy for the next phase of decentralization.
- The activities of the KPK, an independent body, have given new impetus to centrally driven reform in various ways:
 - a. The KPK’s responsibilities include monitoring the governance of state institutions.

Although the Commission has no authority to reorganize government bodies itself, it can and does advise the President on such issues. In addition, it can use its powers of investigation to compel departments and agencies to improve their management and undertake personnel and other reforms aimed at enhancing accountability and transparency. Its prosecution activities have apparently had considerable impact and are even discouraging senior civil servants from participating in projects and other activities that have traditionally provided extra income. This represents an important change in behavior, which may be changing incentives and attitudes towards reform.

- b. The KPK is a new organization and as such has decided to make itself an example or pilot of good governance and sound management. Presidential Regulation PP 23 enables the KPK to manage its finances and personnel outside the normal Gol framework and it has introduced performance management and other innovations. This sets an important precedent for improved governance and management. Unfortunately these measures are not yet fully implemented and at least one KPK official has recently been charged with committing bribery in the course of an investigation.
- At a Cabinet meeting on 15 February 2006 the President endorsed a proposal for fundamental reforms prepared by the KPK and the Partnership that would start with pilot projects; the Supreme Court, the Attorney General's Office, Customs and the Ministry of Trade have all been mentioned as possible candidates for pilots. The KPK and the Partnership are presently working on a revised proposal to be presented to the President in the near future.
 - The reform program would, according to some reports, be led by a small Steering Committee with representatives from Menpan, the State Secretariat, Finance, the business community and civil society. It would be chaired by an eminent figure from outside the bureaucracy. The steering committee would be supported by a technical team based either in the Presidency or the Partnership. The exact nature of these arrangements (mandate and objectives; location of the technical team; oversight; management; reporting lines) and their degree of independence from the regulatory agencies are not yet clear, as various proposals and rumors are still circulating.
 - The Minister of Finance has set up a task force to design a new remuneration policy for state officials. Considerable technical work has been completed and the World Bank has

offered to provide more assistance. It is not yet clear whether any decisions on policy will be taken in time to be included in the 2007 budget. This is an important initiative and shows commitment to reform. The Minister has also indicated that, once this study is completed, it will be followed by remuneration reform for civil servants.

Taken together all these initiatives are encouraging developments; they also enhance the timeliness and potential impact of the findings of this report. The following aspects of the ToR for the first phase are particularly relevant in the present circumstances and will be the focus of this assessment (they are also treated in the ADB report mentioned above and in the Partnership's proposals).

- Recommendations concerning the prerequisite –political leadership, technical skills and management at the central government and local government level – that would be essential for successful implementation.
- Detailed recommendations on the political oversight, organization and management of such a reform effort, including identification of the roles of the various stakeholders (Presidency, State Secretariat, parliamentarians, regulatory agencies, line ministries, MoF, local governments, the Partnership and major interested donors, civil society and the private sector, and public sector unions.)
- A description of the various types of reforms (organization, personnel, finance) that may be possible.

These are complex and difficult issues for any government to address; the analysis that follows will attempt to make recommendations based both on the unique circumstances that prevail in the Indonesian case and on the lessons of international good practice. It may prove useful to begin with the latter, in particular those lessons which would seem to have the greatest relevance for the Indonesian situation.

CHAPTER 5

LESSONS FROM INTERNATIONAL GOOD PRACTICE

The major international lessons attempts to plan and implement reforms elsewhere may be summarized as follows:

Key Points

- Administrative and civil service reform, although often presented as a technical matter of management instruments and increased efficiencies, is in fact a profoundly political issue affecting the balance of power among various actors – civil servants, ministers, legislators, and the central core of government – as well as among agencies, interest groups, and citizens. Resistance may come from politicians, civil servants, other interest groups that fear their influence will diminish and legislators who worry that reform will diminish their power. Reforms designed to improve public administration will produce winners as well as losers; various interests may be mobilized for or against sensitive reforms like improving the professionalism of civil servants, changing the profile of the civil service, or granting greater autonomy to local governments.
- The nature of the constitution and the political system will affect both the agenda for reform and its outcomes. Institutional and regulatory complexity may provide more opportunities for reform proposals to arise but it also provides for a greater number of potential opponents and may stall or even prevent reform from being implemented. Thus reforms have generally gone farther in politically less fragmented systems like the Westminster (British) example where, once Cabinet decides, the points of resistance are weak.
- Countries may choose between comprehensive (whole of government) reforms and a more step-by-step approach. Experience indicates that countries with a fair and transparent electoral process and organized pressure from a literate and well-organized civil society are more likely to succeed at comprehensive reforms. Usually this has happened in middle income countries where the core state institutions that provide the motiva-

tion for reforms have not been “captured” to any significant degree (individuals, groups or firms both in the public and private sectors have few opportunities through bribing to influence the formation of laws, regulations, decrees and other government policies to their own advantage). Low income countries tend to suffer from high levels of *state capture* by elites and interest groups, informal behavior and weak governance.

- Most low-income countries and their donor partners have failed to sustain attempts at broad or comprehensive reforms. A World Bank evaluation shows that about two-thirds of all such projects have proved less than satisfactory in crucial areas like down-sizing, salary reforms, decentralization of services, reduction of the wage-bill and the implementation of codes of ethics. *Above all, the rationale and objectives for reform were not widely accepted, nor were they based on a constituency for reforms at the political level or within the public at large* (See Civil Service Reform A Review of World Bank Assistance, August 1999).
- The illustrations above have highlighted the “natural” proponents and enemies of particular administrative and civil service reform programs. *However, mobilizing support is also about identifying constituencies that would potentially support reform and convincing them through various forms of publicity and promotion that the reform is worthy of public support.* Creating broad societal support for reform is a powerful weapon to disarm opponents of reform.

Lessons about strategies

What can countries with weak governance and high levels of informal behavior do? A two-pronged beginning is best:

- Develop a gradual approach in which the reform of basic institutions and functions takes precedence; once the latter are ensured, then others may be addressed. It took, for example, about 15 years for Malaysia to complete the first or “institution-building” phase of its reforms, including: creation of a strong technical unit in the Prime Minister’s Office; a determination of which services to centralize or decentralize; reforms to personnel management and pay; and key reforms to financial management to strengthen performance and accountability.
- Start with the essentials: strengthen establishment control and management, which is the basis for all other civil service management functions; make recruitment competi-

tive and rigorous; and close the gap between informal behavior and the actual rules and procedures.

Lessons regarding oversight and management of reforms

- Many leaders have attempted to carry out civil service reforms without adequate political, technical or management preparation and by neglecting to involve key stakeholders. By underestimating the complexity of the challenge, they have failed.
- Reform requires both political decision-making and detailed technical analysis about sensitive and contentious issues (the purpose, size and cost of the state; the most effective and efficient approach to devolution, de-concentration, or decentralization; the redefinition of organizations and positions and related personnel changes; how to enhance the performance of staff through reforms to classification, remuneration and other personnel policies).
- A serious reform effort creates exceptional circumstances; therefore, it requires exceptional and transparent political and management arrangements that inspire confidence among all stakeholders and that are as politically neutral as possible. *Regulatory agencies and line ministries that manage the routine administration of the civil service are not suited to planning and managing reforms. Indeed, since they may be targets of reform themselves, it would be a conflict of interest for them to plan and manage such efforts.*
- Serious reforms to the civil service, as stated above, are highly political in nature; yet they also entail difficult policy decisions about technical matters (structure and organization; remuneration; devolution of authority). Political commitment is a necessary but not a sufficient condition for successful reforms. Commitment needs to be institutionalized in a high-level political oversight and policy-making body such as a cabinet committee, supported by a technical reform unit outside the bureaucracy at the highest political level.
- The political level requires guidance about the impact of technical choices and options if it is to make decisions that are both politically realistic and technically sound. The technical work is highly specialized and requires a degree of international expertise in order to ensure that decisions about reforms are based on accurate information and data and that the analysis is rigorous.

CHAPTER 6

KEY ASPECTS OF THE INDONESIAN SITUATION

The problems facing the Indonesian bureaucracy and the challenges they pose for any reform effort are well documented and will not be repeated in detail here. This section focuses rather on the most fundamental or strategic problems of the local context that would have to be addressed in any systematic reform effort:

- Indonesia is a unitary state in the European tradition; the unity and indivisibility of the state constitutes a fundamental pillar of the nation-building that started in the 1950's based on the principles of the Constitution of 18 August 1945. Public law remains the dominant approach to public administration in Indonesia. The poor quality of much legal drafting, however, combined with the sheer volume of new laws and regulations, has resulted in a lack of clarity about authority and responsibilities that undermines the stability of the system.
- Although to some degree, the powers of the President and the executive branch are constrained by the Supreme Audit Agency, the Supreme Court and Parliament, the President nevertheless has considerable authority that could be used if a decision were made to change the legal and regulatory framework as part of a civil service reform. For example, the President may refuse to sign regulations or to cancel ones he has already signed. He can even amend laws retroactively (*Perpu*), as was done in the case of certain electoral procedures contained in Law 32/04.
- The state was highly centralized until the so-called "big bang" decentralization started in 2001 (Law 22/99). It could now be described as a regionalized unitary state. Decentralization, which it is important to note is the only major reform effort ever attempted in Indonesia, was a political phenomenon of tremendous importance and its final consequences are still not clear; in addition, hostility to decentralization and attempts to draw back power to the central level persist (cf. in the education and health sectors).
- A lack of clarity remains about the rationale for and the purpose of decentralization, as well as over the mandates of different levels of government. Before the implications of

Law 22/99 had been digested and the necessary supporting legislation and procedures completed, Law 33/04 was enacted, thereby sowing still more confusion and uncertainty. Progress in adjusting other key laws and regulations in the light of decentralization (see matrix of legal texts currently under preparation) have been slow and are far from complete.

- Decentralization has triggered a prolonged struggle for regulatory authority, power over resources and access to rents among the various actors: central regulatory agencies; local governments; *sectoral* ministries; and the local and national parliaments. This struggle for management and regulatory powers continues unabated. The rules of the game remain incomplete as well as unclear and are constantly shifting; overlap and duplication of effort at the national and regional level remain a problem. The rapid pace of change and competing interests have resulted in an unfinished agenda and a lack of clear procedures, thus slowing implementation of the new responsibilities.
- The management problems of the civil service are aggravated by the highly fragmented regulatory environment, especially in the case of personnel and organization. The emergence of the Ministry of Home Affairs as a major player since decentralization has aggravated what was already a fragmented regulatory environment and increased competition among agencies.
- The regulatory and management framework is characterized by a traditional rules based culture within a closed career system that does not ensure transparency, accountability or consistency in the management of personnel. There is little results based management and in practice no link between pay and performance. The efficacy of existing procedures has been undermined by rampant neglect and abuse of the rules, as well as by a dysfunctional remuneration system and a unique classification method that is skewed in favor of those holding so called structural positions. Widespread patronage and rent-seeking, combined with little enforcement of sanctions, have seriously undermined the accountability of staff and managers.
- The fragmentation of responsibilities for routine management is accompanied by an absence of any high level executive oversight for civil service matters and for reform in particular (neither the Ministry of Law and Justice, the State Secretariat, the Presidency nor Cabinet is currently ensuring that laws, regulations and procedures are coherent and compatible). Indonesia may be a unitary state but since decentralization the state has failed to use its top-down authority to design coherent or consistent policies and to en-

sure that these be implemented by the appropriate levels of government. *If the Gol were to attempt to launch reforms in these circumstances, the effort would fail: there is currently neither the required political oversight nor the technical capacity to address in an integrated way strategic questions like the role, priority functions, personnel requirements and cost of the state and its optimal organization and management.*

- Finally, the experience of decentralization strongly suggests that any major reform to the existing system at the central level would be a highly contentious issue and that reforms would need to be managed from the top and outside the existing regulatory framework in order to have any chance of succeeding.

In short, even a cursory glance at the above in the light of international experience shows that the Indonesian context is a daunting one for reformers: the political struggles triggered by decentralization; the constitutional and legal environment for routine management and the lack of a structure for reform; the fragmentation and complexity of the institutional context (both political and bureaucratic), which provides ample opportunity to frustrate reforms; and the capture of state institutions by various elites and interest groups in a context where corruption is the norm rather than the exception, accountability is low and management practices are largely informal. Indeed, Indonesia shares many characteristics with low-income countries that suffer from weak governance and where attempts at ambitious and/or comprehensive reforms have usually failed.

Essential prerequisites for launching reforms

Now that there is some concrete movement in favor of reform at the highest level and among some powerful stakeholders such as the KPK, it is all the more essential to stress that, without the right approach, any reform effort will not succeed. There are two key sets of prerequisites in the Indonesian case: institutional arrangements (political and technical) and key preliminary measures that must be in place before the reform is launched.

Institutional Arrangements. As emphasized above, reform must be driven and managed from the top and well “above the fray” of regulatory, *sectoral*, regional and other special interests that could potentially stop it or exploit it to their own advantage. Above all, any new reform move-

ment must not be captured by the regulatory agencies, since it is the fragmented and unstable regulatory regime that is largely responsible for the current difficulties in implementing decentralization, as well as for the long-standing failure to achieve even modest performance improvements at the central level. Strong oversight and clear, transparent management of implementation will be required from the very beginning. It will be crucial to impose and enforce authority in a context where, after years of informal behavior and rent seeking, accountability mechanisms have been severely weakened.

The crucial importance of this principle, while clearly proven by international experience, has not yet been fully acknowledged or accepted among key players in the Indonesian case. The reform proposals submitted by the various regulatory agencies (Annex 3) recommend oversight arrangements that are weak and part-time such as coordination through inter-ministerial committees. Nor do these proposals call for enhanced technical analysis and advice from outside specialists in the planning and sequencing of reforms.

For example, although the governance reform initiative of the KPK advocates setting up a team under the President, the mandate and degree of independence of the team are not clearly spelled. It is not yet clear whether the President and Cabinet as a whole (certain ministers are in favor of a more coherent reform effort) grasp the depth and complexity of the political, technical and implementation challenges posed by the Indonesian situation.

Recommendations on political oversight, organization and management

- Create a small (three or four member) high level committee (for example, a mixture of Cabinet members like the Minister of Finance and others like the Chairman of the KPK) chaired by the President and carefully define a robust and transparent terms of reference. The latter should focus on articulating a clear political and economic rationale and objective for the reforms; recommending how best to involve stakeholders in the effort; explaining the initiative to the public at large; approving proposals related to the reform program and its implementation and ensuring the necessary political support and actions (for example, regulations, legislation, contacts with Parliament, local government, etc.)
- Devise a mechanism such as an “advisory council” in order to consult formally with the key

stakeholders in and outside Government.

- Brief the donor community on the importance and nature of the reforms and encourage the creation of a small donor working group.
- Set up a technical group/unit in the Office of the President and ensure its legal and bureaucratic independence from the ministries. The group should consist of economic, legal and personnel management and administrative reform specialists, supported by experts on change management and stakeholder participation. Both local and international expertise would be required. The unit must be given a strong mandate: access to all required data, legislation and other necessary documentation; easy access to the President's top staff; and authority to speak on behalf of the President with the donor community.
- The mandate of this group would be to recommend an approach (strategic framework) based on a thorough analysis of the Indonesian situation and an identification of priority areas and appropriate sequencing. The content and time horizon for the strategy and the work program (see below) would be influenced by political (cf. the 2009 elections), technical and capacity considerations.
- Mobilize the President and Cabinet to ensure full cooperation with this group from senior officials and the advisory council.
- Impress upon donors that, if they want to help with the reforms, then they must realign their programs in accordance with the Government's priorities or aid will not be welcome.
- Help the President and the members of his high level committee to define and announce clearly their commitment to reforms and to articulate the rationale, objectives and priorities.
- Bring international experience to bear and organize a regional workshop on reforms (cf. the leadership of the Prime Minister and his Office and the clear rationale and highly focused management of the reform program in Malaysia).
- Organize informed debate among the principal stakeholders on the general approach and on priority actions in the hope of reaching some consensus on the broad agenda.
- Write a detailed, sequenced work program for the first phase of the reforms; within the process, devise options and scenarios and discuss these with the high level committee and the advisory council.

Key Preliminary Measures

- These measures would complement the creation of necessary oversight and technical arrangements. They are necessary for successful launching of the reforms. In addition, they will send a strong initial message about the seriousness of the effort.
- The rationale and objectives of the reform must be articulated clearly and explained to all stakeholders through a well-organized campaign that includes extensive dialogue with the key interest groups affected. The Government must make very clear what exactly it expects to achieve (for example, a more efficient use of scarce state resources; and better services through enhanced accountability combined with better incentives for staff), how and in what time-frame.
- In doing the above, the Government needs to emphasize that the mistakes of the so-called “big bang” approach to decentralization will not be repeated again. This time the reforms will be well prepared, gradual and sequenced within a coherent and transparent framework and time-frame. The basics and the prerequisites will be addressed first.
- In reviewing the regulatory framework, this reform will affect the continuing decentralization efforts; it needs to be emphasized that the latter are also subject to review and to a moratorium if necessary.
- It should be made explicit from the outset that the legal and regulatory framework itself will be subject to reforms that may result in a realignment of functions among fewer agencies. In the meantime, the status quo will not suffice: legal measures presently under consideration must be reviewed and if necessary delayed so that, once launched, the reforms stay on track.
- Given the above, strong political leadership by the President will be needed to impose a “cease fire” on the competing regulatory and bureaucratic interests. Required measures must include a moratorium on all new legal actions that could potentially disrupt the reforms, and a review of all new legislation and regulations currently under preparation, including that related to decentralization. The reform team must enjoy the right to advise the President on legal matters and to advocate, if necessary, that he not sign regulations prepared by the bureaucracy that could impede the reform process.
- The status of existing reform proposals and activities (cf., from the KPK) must be clarified, as well as their relationship to the new program. It may be necessary to suspend certain activities while the reform strategy is developed.

Legal and regulatory reform for civil service management: an immediate beginning and a “quick win”?

As stated above, legal measures presently under consideration must be reviewed and deferred if necessary so that, once launched, the reforms stay on track.

Yet attempts to create a strong top-down reform based on the principles and administrative arrangements outlined above may be delayed or not fully implemented. Thus reformers in the Gol and the donor community need to consider other approaches and alternative ways of launching reforms that could keep the momentum alive in the interim while attaining concrete results in the short to medium term.

One way would be for the President to take immediate measures to improve oversight of the preparation of legal texts; and donors could provide technical assistance to develop better policies and instruments, as well as to improve legal drafting.

A good example is the crucially important civil service law, which needs to be made compatible with the decentralization laws; in addition, the proposed law on teachers and lecturers needs to conform to the other two.

Such an initiative could have a positive impact in the short term:

- It would reaffirm the power and the obligations of the unitary state as embodied by the President to exercise his full authority based on the law. It would send a strong signal that accountability is at the core of good governance and that the President intends to bring behavior back into line with the laws and regulations. It would also complement and reinforce the efforts of the KPK to eradicate corruption.
- It would show that the President and the Gol are serious about better civil service management and that the Government intends to use its existing prerogatives to review and amend regulations and thereby render the legal context more coherent and transparent.
- It would send a strong signal by demonstrating in a concrete way to civil servants and politi-

cians alike that the implementation of reforms will take the form of tightening compliance with existing regulations while more ambitious changes are planned and prepared. Such a move would be fully compatible with a more ambitious reform effort that could start at any time.

- By emphasizing rigor in both legal drafting and the development of better policies and instruments, it would i) improve the technical skills of those responsible in the regulatory agencies, the Ministry of Law and Justice, the State Secretariat and the Presidency; and ii) re-establish the credibility of the institutions and individuals responsible for this area.

CHAPTER 7

IDENTIFICATION OF MAJOR POLICIES AND TECHNICAL INSTRUMENTS FOR REFORM OF PERSONNEL AND ORGANIZATION; REVENUE AND EXPENDITURE

Introduction

This part of the report summarizes the major policies and technical instruments as actions to be undertaken in civil service reforms.

1. *Political oversight, technical support and program management*

- The President to assert political leadership
- Establish top level political oversight arrangements (a small group including one representative of a regional government) and a technical group equipped with legal, economic and public management skills and placed outside the existing regulatory agencies
- Freeze issuing of new regulations and laws by ministries and agencies
- The President to define a clear vision and purpose for reform, reiterate GOI commitment to decentralization and encourage debate about the rationale and objectives
- Establish a technical group to define strategy, including options and trade-offs
- Organize political and public debate on these issues to reach an understanding of the issues and eventually a consensus

2. *Regulatory Issues and Institutional Responsibilities*

- Define the mandate and functions of the legal and regulatory framework

- Apply functional analysis to determine what institutional set-up would best meet these goals
- Rationalize current sharing of regulatory responsibilities and management functions among existing agencies, and abolish or merge agencies as required and or feasible
- Regarding the above: political and bureaucratic realities may lead to partial reforms of certain functions; for example, personnel, finance etc.
- Implement the new arrangements based on coherent legal texts
- Review the decentralization laws and other relevant legislation, regulations and procedures in order to remove existing barriers and anomalies
- Redefine decentralization through a sound legal and regulatory basis accompanied by the definition of responsibilities and detailed procedures at all levels of GoI
- Begin work on setting targets for the wage-bill as a macro-economic variable in order to ensure that the reforms take place within a firm budget constraint

3. Strategy and Sequencing

As the initial tasks outlined above are undertaken, those in charge of the reforms will need to start thinking about the sequencing of the reforms. This will prove a difficult and sensitive undertaking and the results will be determined by political realities and technical considerations. The following issues will have to be taken into account:

- Certain reforms are one-off activities (for example, reorganization and right-sizing) that are time-bound, radical and sensitive; these will probably take place early in the reform process.
- Other reforms are permanent and designed to implant new policies for all personnel across at the central government and local government levels in key areas (for example, replacement of the pay and grading system and renewal of the routine personnel management functions and procedures). These will take a long time to develop, discuss and implement, as many central policies and procedures are obsolete and will need to be redesigned from scratch in cooperation with representatives of regional authorities.
- An important distinction must be made between the *timing for the preparation* of new policies in such areas and *the sequencing of their implementation* (for example it may be decided that preparation of a complex task like a new pay policy should begin on a prior-

- ity basis; this is a separate decision from the timing of its introduction).
- In addition to political considerations, the timing and sequencing of reforms should be based on an analysis of their potential relative impact in light of the objectives of the program; how the regions view the priorities in areas where they essentially implement national policies; how the relationships between reforms mandates sequencing; the capacity of managers to absorb innovation, and the need for evaluation throughout the process.
 - The literature on reform experiences distinguishes between comprehensive and partial or gradual approaches to reform and stresses that countries with difficult governance contexts and limited management capacity have seldom succeeded in introducing ambitious comprehensive programs of reform. Such programs usually feature the simultaneous reform of key constraints through activities like functional analysis, restructuring, right-sizing, matching people to the new structures, remuneration reform, and retrenchment or voluntary departure. Experience shows that this approach is not suitable for most countries. *It is better to aim at comprehensiveness over the long term through a gradual approach in which the reform of certain basic functions takes precedence.* Once the latter are ensured, then other functions may be addressed. It took, for example, about 15 years for Malaysia to complete the first or “institution-building” phase of its reforms, including; creation of a strong technical unit in the Prime Minister’s Office; a determination of which services to centralize or decentralize; reforms to personnel management and pay; and key reforms to financial management to strengthen performance and accountability.

4. Personnel and Organization (P&O)

Priority Reforms in terms of policies, functions and tools

Despite decades of studies and recommendations from within Gol and from the donor community, the well-documented weaknesses of the P&O system, policies and instruments remain largely unchanged. The Diagnostics and Roadmap studies from NTB and West Sumatra clearly indicate the many inadequacies, of which the most egregious are:

- Ranking of civil servants (PNS) suffers from a lack of national position classification, job evaluation and job description.

- Distortions and inequities which are created by the structural position system.
- Allowances and other benefits linked to structural positions discourage staff from seeking out or remaining in functional posts.
- Unequal availability of non-transparent payments and benefits, particularly for structural staff within certain so called “wet” ministries. Such benefits are unrelated to performance.
- Overstaffing, particularly of echelon staff and in lower level posts.
- A mismatch between needed skills and the actual qualifications of many staff currently in post.
- An almost total absence of human resource planning.
- An inadequate early retirement regime that has kept overstaffing in place and forced managers to rely on attrition as the only viable tool for reducing numbers.
- Weak regulations concerning the reorganization required as a result of decentralization
- Outmoded and/or inappropriate personnel instruments (cf., job classification, job descriptions, job analysis; credit point system; DP3) that are not geared to performance management. Use of certain instruments for tasks to which they are not suited (using job analysis to define needed posts).
- Provision of training by central institutions based on categories of staff rather than on locally determined needs.

An alternative categorization: Priority reforms in terms of objectives

In order to emphasize the rationale and ultimate objectives of reforms, it may be useful to define and cluster the functions in terms of their concrete *objectives and expected results* rather than as purely technical functions. This approach should also help to clarify thinking about sequencing. In the area of personnel, for example, the Diagnostic and Roadmap for West Sumatra stresses the importance of addressing key objectives such as “the right person in the right job”. This approach would mean prioritizing clusters of related activities that would require reform in order to meet such objectives such as:

Priority I: The right person in the right job

Issues to be addressed:

1. Design Job Classification and grading of the jobs

2. Design Job descriptions including competency requirements
3. Identify key elements for a HR database and planning tool; acquire and introduce the software
4. Match individuals to positions with the help of the planning tool
5. Design policies for redundant staff including an early retirement scheme, outsourcing and outplacement
6. Consider appointing contract staff for vacant posts after match is completed based on years on contract, merit, performance and skills
7. Recruit and appoint transparently and consistently for specific vacant posts based on merit and skills

Priority II: A transparent and equitable remuneration package for all

Issues to be addressed:

1. Design pay and grading systems in relation to job classifications under number 1
2. Design a complementary local remuneration package based on performance
3. Design a policy for the transition from the old to the new grading system based on equity, merit and performance

Priority III: Performance management for all

Issues to be addressed:

1. Design a performance appraisal method based on the new job descriptions for bi-annual evaluation
2. Design a policy including criteria for advancement and promotion based on performance, merit and skills
3. Design criteria and procedures for exceptional performance related to extra pay

The above suggest that the following technical reforms are required over the medium term:

- A new classification and grading system
- A new remuneration system
- Job descriptions
- New and transparent organization and personnel instruments geared at ensuring accountability and performance management
- Human resources planning tools
- Provisions for early retirement to facilitate right-sizing and the matching of individuals to

job positions

- Guidelines for reorganization based on an identification of government priorities and the use of appropriate tools such as functional analysis
- Provision for periodic re-organization based on local needs and flexible instruments
- A code of conduct and integrity pacts
- Systematic improvements to the management of work, including better delegation and accountability instruments
- Enhanced discipline and attendance
- The introduction of behavioral change in order to reduce the gap between formal rules and actual/informal behavior

Priority IV: Revenue

In addressing the fourth priority, sound local own revenue (PAD) management the issues are:

1. Review current PAD revenue
2. Conduct a study to (1) estimate the PAD capacity; and (2) explore improving PAD capacity
3. Review local regulations for local taxes and charges
4. Design instruments to improve the database for local taxes and charges
5. Develop medium term revenue planning
6. Develop/improve systems and procedures of revenue collection and administration

Priority V: Expenditure

In addressing the fifth priority, redesigning and improving local financial administration the tasks are:

- Review local regulations for local financial administration: i) assess and identifying the strengths and weaknesses of the current local financial administration system and its procedures, and ii) assess the gap between current local regulation and the changes required by central regulations.
- Redesign the local financial administration system and procedures to: i) comply with the new central regulations; ii) support the new organization designed by the pilot on organization; and iii) be more accountable, more effective and efficient in supporting the decision making process.
- Assess the implications of the new system and procedures for: i) personnel qualification

and skills needed; ii) training needs; iii) resources needed to run the new system.

- Introduce new software to support local financial administration.
- Prepare a training manual for financial officers of all dinas with necessary skills to manage the allocated resources.

ANNEX 1

Matrix of Laws and Regulations under Preparation

LEGAL TEXT	RESPONSIBLE AGENCY	STATUS	COMMENTS
Amendment of Law 43 (CS Law)	Partnership-STIA (LAN Graduate School)	Under discussion. See note attached	Need to reconcile with Law 32/04 on decentralization
Law on Teaches and Lecturers	Ministry of National Education	Draft at President's Office	Enhance professionalism and job security; specifies allowances and other benefits.
Law on Government Organization	Parliament	Being discussed in Parliament	
Amendment of Law 11/69 on Pensions	Partnership/BKN	Draft policy paper	
Replacement of PP 08 on Local Government Organization	Menpan/MoHA	Draft under discussion in MoHA	Based on authorities rather than on functions
Replacement of PP 25 on Distribution of Authorities among Levels of Governments	Menpan/MoHA	Draft under discussion in MoHA	See draft summary
New PP 63/05 on the Management of KPK personnel	KPK	Issued	Under implementation. Non-traditional performance based approach
Amendment of PP 10/80 on DP3 (performance appraisal)	Menpan and BKN	Draft	More performance based than before
Amendment PP 52/79 on departure of PNS, including early retirement	Partnership/BKN	Draft policy paper	
Amendment of PP 30/80 on Discipline	BKN & Menpan	Draft	Revised criteria for sanctions

ANNEX 2

Draft of New PP 25 Compared to Existing Text

Topic	PP 25/2000	Draft of a New PP
Title	PP on Authority of (Central) Government and Province as Autonomous Region	PP on Division of Governmental Affairs/urusan among Central, Autonomous Provincial Government, and Autonomous Kabupaten/Kota Government
Authority	<p>Central Government authority is mostly in setting policy that covers norm, standard, criteria, and procedure, and limited in implementation of authorities with national coverage</p> <p>Provincial Authority: in governmental sector/<i>bidang</i> across Kabupaten/Kota in specific sectors, comprises of: planning and directing macro regional development, training in specific sector, potent human resources allocation, research with provincial coverage, management of regional harbor, control of living environment, trade and culture/tourism promotion, handling of transferable disease and pest in plantation, and regional spatial planning authority that is not/not yet carried out by Kabupaten/Kota</p> <p>Kabupaten/Kota' authorities according to agreement</p> <p>International agreement and commitment made by Central Government applied to regional/local government</p> <p>Agreement and cooperation by regions with foreign institution must not in conflict with similar agreement and cooperation made by Central Government</p> <p>Central Government holds the right to take administrative sanction to the RG/local government for neglecting and/or breaking the enforcement of laws and regulation</p>	<p>Concurrent affairs are divided among all governmental levels proportionally based on principles of externality (area effected), accountability (to avoid duplication), and efficiency. All to be synergized toward social welfare and democratization as the essence of decentralization policy.</p> <p>Affairs under Regional and Local authorities comprise of obligatory that related with basic services such as elementary education, health, living environment, transportation, population, etc., and optional that related to core competence. All to be focused on the accomplishment of social welfare in accordance to regional condition, potential and specification.</p> <p>Beside obligatory and optional affairs all level of governments carry out "left out" affairs (<i>vrij bestuur</i>).</p> <p>Regional and local government will be empowered to improve regional and local government capacity.</p> <p>Interconnectedness and interdependency must be reflected in the implementation of affairs of different level of government within the framework of the Unitary System of the GoI.</p>

ANNEX 3

Matrix on Reform Options Leading to Potential Reform

A. Political and Technical oversight and management				
	Possible priorities	(political and technical) Feasibility: L = low M = medium H = high	Key actors: M = Menpan B = BKN H = MOHA F = MoF L = LAN LG = Local Gov O = other	Reform option: P = pilot G = gradual C = comprehensive
	President to assert political Leadership	H : Written statements, public addresses.	O : Special agencies (KPK, partnership)	P : (example: HRM of KPK as a national pilot project of CS Management)
	Establish a focal point for reform at political and technical level and outside The existing agencies	Political :H, Technical/Bureaucratic level *) : M Outside:H (Parliament, NGO) *) Heavy sectoral point of view.	O : neutral & independent committee	P
	Freeze issuing of new regulations and laws by Ministries and agencies	L : -New regulations are needed to implement law - Urgent need to revise some unfit laws and regulations.	all	C
	President to define broad objectives for reform & encourage debate	L : - Cultural background - Insufficient technical support.	O : T.A from outside	G : Need of cultural adjustment, Institutional&HR capacity Building
	Technical group to define	L : Low internally, need outside support.	O	C

	strategy, including options and trade-offs			
	Organize political and public debate on these issue to reach consensus	M: not all stakeholders familiar with the issues to be debated	O	G: need of capacity building (politician, bureaucracy, community)
	President to reiterate GOI commitment to Decentralization	M: not all stakeholders have the same vision about decentralization	all	G: Shared pilot by all stake holders
	Review: the decentralization laws and other relevant legislation, regulations and procedures in order to remove existing barrier and anomalies	L: Newly enacted law and hasn't been followed by new government regulations	all	C
	Confirm decentralization through a sound legal and regulatory basis accompanied by the definition of responsibilities And detailed procedures at all level of GoI.	See above as prerequisite	--	--
B. Regulatory Issues and Institutional Responsibilities				
	Possible priorities:	(political and technical) Feasibility: L = low M = medium H = high	Key actors: M = Menpan B = BKN H = Moha F = MoF	Reform options: P = pilot G = gradual C = comprehensive

			L = LAN LG = Local Gov	
	Prioritize goals within the legal and regulatory framework	Political: H = Community demand for reform Regulatory: M = inconsistency in some regulation Technical: L = inability to absorb views of Stakeholders	all	C: Leading actor must be define
	Apply functional analysis to determine what institutional set-up would best meet these goals	H - Technically High M - Constrained on <i>sectoral</i> interests (such as in determining leading actor)	all	C: Inter-ministerial team
	Rationalize current sharing of regulatory responsibilities /management functions among Existing agencies	M: Have to accommodate sectoral interests within the framework of national interest.	all	C
	Re the above: political and bureaucratic realities may lead to partial reform of certain functions: personnel, finance, etc Implement the new arrangements based on coherent legal texts.	M - See above	Core stakeholders (which similar core function).	P
C. Technical functions				
	Possible priorities	(political and technical) Feasibility: L = low	Key actors: M = Menpan B = BKN	Reform options: P = pilot G = gradual C = comprehensive

		M = medium H = high	H = MOHA F = MoF L = LAN LG = Local Gov O = Other	
1. Organization	Functional review	M: - Functional inflexibility - Limited space to maneuver - Limited technical capability	LG O	P
2. Personnel	Human Resource Planning (HRP) (incl. right-sizing policy)	M: - Menpan has no tool to assess "formasi" based on human resource planning method - Room available for local government to develop their own HRP but insufficient technical capability	LG BKN O	P: need TA develop HRP
	Recruitment	M: - Closely related with HRP - Room available for local government to develop their own recruitment incl. the tool need	LG BKN O	P
	Human Resource Development (HRD) (incl. placement, promotion, transfer, training)	M: - Closely related with HRP - Basic prerequisite (position classification, staff appraisal, standard of competence, career planning, training need assessment model) has to be established.	LG BKN (regional office) O	P
	Performance based remuneration (through the job evaluation)	M: - Basic salary is nationally regulated - Room for local government to develop incentive system	LG BKN (regional office)	P

	technique)		O	
	Performance Appraisal	M: - Closely related with HRD - DP3 does not related with performance - local government develop DP3 supplement - Assessment center method applies for strategic position.	LG BKN O	P
3. Management of personnel and accountability	Introducing Performance Management	H: High commitment of Central Government	Other	P
	Code of conduct and Integrity pacts	H: - Code of conduct based on PP.42/2004 has not been implemented - local government may develop their own code of conduct based on PP.42/2004 adjusted to local characteristics including the applications of integrity pacts.	LG O	C
	The management of work including delegation and accountability instruments	H: - Based on the top management goodwill - Establish standard of competence - Establish staff appraisal	LG	C
	Discipline	L: Weakness in PP 30/1980, cause subjective judgment in enforcing discipline, that resulted in opening chance of civil servant to avoid disciplinary action.	Central Government (to amend the PP)	--
	Introduction of behavior change in order to reduce the gap between formal rules and actual/informal behavior	H: Menpan has set guidelines the corporate culture for civil servant	Menpan LG O	P

ANNEX 4

Example of Diagnostics and Roadmap including reform options

1. KABUPATEN SOLOK - FINANCE- Expenditure

No	Functions	Questions	Responses	Problem Identification	Stakeholder
1.	Budget Planning, Policy Formulation, Execution and Monitoring	What types of budgets do you use? (for example, line item budgets, performance budgets). Are they linked to program objectives and performance indicators? If yes, how do you actually link the budget and the performance?	<p>Since 2003, Kabupaten Solok has used performance-based budgeting in line with Kepmendagri 29/02.</p> <p>They recognize the weaknesses in the actual practices. In many cases, the relation between the budget for activities and the performance indicators are not clear.</p> <p>Budget preparation starts with participatory planning. The budget planning begins with Nagari discussions (which bring all stake holders to a discussion forum).</p>	<p>The links between program/activities and performance indicators are often unclear. Indirect expenditures (such as for salaries of civil servants (PNS) have not been apportioned to activities.</p> <p>The Kabupaten has used participatory planning process to improve the budget allocation and to be more responsive to local needs. Specifications of Minimum Service Standards (SPM) for all functions are incomplete. Standards for spending assessments to evaluate the proposed budget (especially for indirect expenditures) are incomplete. Improving budgetary planning entails improvements to Kepmendagri 29/02, and strengthened human resource capacity in planning and implementation.</p>	CG & LG

No	Functions	Questions	Responses	Problem Identification	Stakeholder
2.		How do you monitor and evaluate budget performance?	<p>Budgetary execution is monitored by several units. The first is by BPKD, which monitors all units (including revenue) by producing monthly and quarterly reports.</p> <p>The second is by the Bappeda (the local planning agency). The third is each Dinas for their respective activities, procurement and capital expenditure. The fourth is by the Development Unit in Setda. The fifth is by the Bawasda (provincial internal auditor), which monitors and audits all units.</p> <p>As a coordinating mechanism, results of monitoring should be reported to the Bupati through the Development Unit.</p>	<p>There are questions about the efficiency, overlap and effectiveness of these multiple monitoring agencies, whereas coordination and comprehensiveness is the key to effectiveness. The capability of the monitoring and auditing officials needs to be strengthened, while better tools and instruments for monitoring need to be developed.</p>	CG & LG
3.		Are you doing an adequate job in developing expenditure plans?	<p>Yes, according to Kepmendagri 29/02.</p> <p>The budget team prepares the general direction of the budget (AKU) as well as the strategy and priorities (SP). It is assisted by representatives of a local NGO.</p> <p>The AKU and SP (as approved by the DPRD) will be used to guide the units to propose their budget plans (RASKs). The RASKs are scrutinized by the executive budget team and consolidated into a budget document.</p>	<p>Weaknesses in Kepmendagri 29/02 cause problems of implementation. As a result, some duplication is inevitable. For example, expenditure for official travel and purchase of goods are in two budget items (general administration and operations and maintenance). In theory, these budget items are for different purposes, but it is very difficult to assess whether both are needed. It is also very hard to distinguish whether the funds have used as indicated.</p> <p>Revisions to this regulation are pending owing to changes in the Decentralization Law and various new Laws regulating local government finance. Some of these Laws are contradictory.</p>	CG & LG

No	Functions	Questions	Responses	Problem Identification	Stakeholder
4.		Do you have sufficient time to prepare, to execute and to monitor the budget performance?	Yes, but the time provided for the preparation of RASKs (budget plans of working units) was too short. A new budget schedule has been agreed by DPRD.	The budget schedule requires strong commitment. If one step is delayed, it can lead to delayed approval of the budget.	LG
5.		Can you avoid overlap in the budget? How?	The duplication in the budget can be limited by performance-based budgeting. However, unclear organizational mandates and job description also cause duplication.	Some vaguely defined programs of units in the local government cause duplicate targets. For example, two units can have their own training programs for the same target group.	LG
6.		What role does the DPRD (local parliament) play in budget policy formulation and approval?	DPRD scrutinizes the general direction of the budget (AKU) and the strategy and priorities (SP). Participatory planning is also used, and DPRD members are included in the process.	Discussions about the AKU and the SP with DPRD can be difficult, due to different perceptions as between the DPRD and the Executive. This can lead to inefficient and ineffective discussions. The quality of the DPRD needs to be upgraded through workshops and discussions.	LG
7.		How does the central government inform local governments that their programs and budgets have been approved?	The requirement for consultations with the province (Law 32/2004) on the local government budget has not been implemented yet.	This has the potential for a conflict between local governments and the Province.	LG

No	Functions	Questions	Responses	Problem Identification	Stakeholder
8.		What percentage of your DAU represents cost transfers exclusively for wage bills?	<p>About 92% of DAU is for personnel expenditure (salaries, benefits, local incentives, and honorarium).</p> <p>Since 2004, Kabupaten Solok has followed a local incentive system that provides additional salary for employees. This incentive is an average increase of about 12% in PNS salaries. This system replaced the honorarium for every activity as currently being practiced by the Provincial Government and by other local governments in West Sumatra.</p> <p>Special Note for Comparison: Data for calculating the 2005 DAU in the MOF indicates that the ratio of total DAU to total salaries of civil servants in kabupaten/kota is about 63% (about 50 trillion for salaries from 80 trillion DAU).</p>	<p>A large number of personnel (more than 5,000) and an expansive organizational structure, have absorbed almost all the DAU. It is possible that in the coming year, personnel expenditure will exceed the amount of DAU for the Kabupaten.</p> <p>The split of this Kabupaten into 2 parts (Solok and South Solok) in 2004 has disadvantaged Kabupaten Solok in its transfers through the DAU.</p> <p>In 2004, the DAU was negotiated with the Central Government and South Solok, assuming that a relatively large number of civil servants would move from Solok to South Solok. In the event, a much smaller number moved, saddling Solok with a relatively large number of civil servants, but significantly less DAU. A new formula has been negotiated, but Solok has suffered a once-only loss in its DAU and been left with redundant staff.</p>	CG & LG
9.		Do you consider deconcentrated funds in your planning? How?	local government has tried to consider all sources of funding in the planning process by asking the units to bring the DIPA (document of program funded by the central government budget) and the list of programs funded by the provincial budget.	The DIPA is usually late and unpredictable. The situation is similar for the provincial programs in the kabupaten. Duplication is difficult to avoid. Central programs are informed directly to the Dinas, by-passing the Bupati.	LG
10.		Are Kabupaten/Kota involved in the provincial budget planning?	Yes, in the annual Provincial planning discussions.	After a program is included in the provincial budget and the budget approved, the Kabupaten/Kota is not formally informed as to what projects/programs are going to be	LG

No	Functions	Questions	Responses	Problem Identification	Stakeholder
				implemented.	
11.		For Kabupaten/Kota: Do you consider the provincial budget in your plan? How?	Yes, see the answer in No 9.		LG
12.		How often do the local governments prepare and approve a supplementary budget?	Once a year. Usually there is also a revision of the DASK (the unit budget document) by Bupati decree.	local government prefers not to have a budget revision since it takes time to get the DPRD's approval. Also, political considerations usually dominate in budget amendments. It is very difficult not to have the budget revision since many things could happen during the second semester of the budget, especially unexpected project/programs and revenues from Central Government.	LG
13.		Are any compliance, performance or financial audits ever conducted?	Internal audits are conducted by provincial Bawasda. External audits are conducted by BPK. In general, the audit practice (internal and external auditors) is concerned with compliance with regulations. The external auditor conducts only financial audits, giving an opinion on the financial report, not on compliance with the performance targets.	Absence of performance audits renders meaningless the local government's performance targets.	CG & LG

Reform Agenda and Suggested Reform Program for Budget Planning, Policy Formulation, Execution and Monitoring

Objective: Increase Public Services While Holding Down Their Cost.

Near-term Steps:

- Strengthen the implementation of performance based budgeting (ABK) by, for example:
 - Reviewing the technical guidance for budget planning and implementation, possibly with the assistance of a technical advisor;
 - Evaluating cost standards regularly;
 - Developing a computerized financial reporting system, including for budget and accounting systems; and
 - Developing standard instruments of analysis to evaluate unit budget proposals (RASKs).
- Strengthen planning, coordination and communication between provincial dinas and kota to reduce overlap in sources of funding.
- Identify the steps and design a policy to harmonize programs funded locally and by the *Dana Dekonsentrasi*.
- Identify steps and bottlenecks in the Budget preparation process to introduce a more realistic schedule; to add more discipline to meet that schedule; and to reduce the need for supplementary budgets.
- Develop a strategy for coordinating donor assistance, preferably using a locally driven approach.

Longer-term Steps:

- Train civil servants in budget planning, budget implementation and value for money.
- Rationalize the number of monitoring agencies, while strengthening the Bawasda, for example: by adding a performance audit role in support performance-based budgeting; and including an assessment of internal controls.
- Upgrade the quality of the DPRD, for example, through international support to the DPRD secretariat.