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Client Alert Memo

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Indonesia employment law update[1]

Reform of Indonesia labour law: the employment protection law increases employee protections

Following Constitutional Court Decision No. 168/PUU-XXI/2023 ("**Decision 168/2023**"), the Government and Parliament were mandated to enact a new standalone labour statute by 31 October 2026 to succeed Law No. 13 of 2003 on Manpower (as amended) ("**Manpower Law**").

On 28 October 2026, the President signed Law No. 27 of 2026 on Employment Protection (the "**Law**"), which was promulgated on the same day and came into force on the date of its promulgation.

The Law revises provisions across multiple areas, including outsourcing, fixed-term employment, termination of employment, and minimum wage.

1. Background

On 31 October 2024, the Constitutional Court issued Decision 168/2023, reviewing the manpower cluster of Law No. 6 of 2023 on Job Creation ("**Job Creation Law**"). The Court did not annul the Job Creation Law or its implementing regulations, but directed the Government and Parliament to enact a new standalone employment statute within two years. The Law now revokes the Manpower Law and the manpower provisions of the Job Creation Law. Government Regulation No. 35 of 2021 on Fixed-Term Contracts, Outsourcing, Working Hours, and Termination ("**GR 35/2021**") remains in force only to the extent not inconsistent with the Law, and the Government is required to issue new implementing regulations within one year of promulgation, that is, by 28 October 2027.

2. Some key changes

2.1 Outsourcing restricted to four service categories with special rules for mining, oil, and state-owned enterprises

Previously, under Minister of Manpower Regulation No. 7 of 2026 on outsourcing ("**MoM Regulation 7/2026**"), outsourcing was restricted to six categories of supporting services, namely cleaning, catering for workers, security, supporting services in mining and oil, workers transportation, and operational support services.

The Law narrows this list to four categories, namely cleaning, catering for workers, security, and workers transportation. "Supporting services in the mining and oil sectors" may now only be outsourced to a subsidiary of the principal in the form of a limited liability company, and for supporting services outside the four general categories, state-owned enterprises may only outsource them to their own subsidiaries. While the Law does not expressly revoke MoM Regulation 7/2026, Article 310 of the Law states that provisions of previously issued implementing regulations of the old Manpower Law would remain in effect unless they contravene the Law. Given the disparity between the provisions of MoM Regulation 7/2026 and the new Law, it is likely that the aspects regarding the types of work that can be outsourced to another company under MoM Regulation 7/2026 have now been superseded by the Law.

Compared to MoM Regulation 7/2026, the Law also increases the severity of consequences of non-compliance with the outsourcing restrictions. Where workers supplied by an outsourcing company are used by the principal for activities that "directly relate to the production process", the employee is considered to have a direct employment relationship with the principal by operation of law. Workers may ask the local district court to recognise this relationship if, after a bipartite negotiation and examination by the labour inspector, the principal fails to implement the direct employment arrangement.

1 This bulletin does not constitute legal advice. If you would like more information on this issue, please contact the individuals listed at the end of this bulletin.

Companies using outsourcing arrangements have one year from enactment of the Law to comply with these new requirements. Peculiarly, the Law also provides that outsourcing agreements entered into before its enactment remain valid until they expire, without clarifying how this interacts with the one-year compliance deadline. Pending clarification in the implementing regulation, there is a possibility that regulators will treat 28 October 2027 as the overarching compliance deadline, even for agreements that extend beyond that date.

Historically, there was a distinction between "outsourcing" and the "subcontracting" of services.[2] The Law tracks the drafting of MoM Regulation 7/2026 closely, which was designed to regulate "outsourcing" in the narrow sense of the supply of labour by one company to another, involving the provision of manpower and not the delivery of defined work or services (subcontracting).[3] The term "outsourcing" or *alih daya* was also used in the Job Creation Law. However, unlike the MoM Regulation 7/2026, the Law does not expressly define outsourcing.

On that basis, this restriction is in theory best read as applying to labour supply and not to service subcontracting, where a contractor delivers defined work or services using its own workforce, equipment, and methodology, and retains full operational control over its personnel.

However, pending clarification in the implementing regulation (which, under the Law, must be issued within a year), there remains a risk that an output-based service contract is not automatically considered to be outside the scope of the outsourcing restrictions.

In the meantime, businesses contracting for services should ensure that any such arrangement does not display the hallmarks of a labour-supply engagement. This means ensuring that:

(i) the contractor retains supervision and discipline authority of its personnel, including hiring, rostering, and performance management;

(ii) remuneration is provided based on defined service deliverables or outputs, not to headcount or man-hours;

(iii) the contractor provides its own equipment, materials, and work methodology;

(iv) the contractor's workers are not integrated into the principal's organisational structure, placed on its reporting lines, or treated as part of its workforce;

(v) the contract includes output-based service levels, performance warranties, and liability for defects;

(vi) the principal retains the relevant intellectual property rights and quality control functions in respect of the activities;

(vii) the contractor possesses the relevant business licence to carry out the contracted activities; and

(viii) the arrangement takes into account and complies with any applicable sectoral regulations.

2.2 Tighter limits on fixed-term employment contracts

Previously, fixed-term employment contracts could be used under GR 35/2021 and the previous Manpower Law for an aggregate term of up to five years, with flexibility as to the number and duration of extensions within that cap. The Law tightens this, reducing the maximum aggregate term to four years under a "2+1+1" structure: an initial term limited to two years and no more than two extensions, each of up to one year. Employers must notify the employee of any extension at least seven days before the contract expires, and fixed-term contracts must still be registered with the relevant manpower office within three working days of signing.

A fixed-term contract that is not made in writing, or that is used for work that does not qualify for fixed-term employment or is permanent in nature, will convert by operation of law into a permanent employment contract. While the Law does not expressly attach the same consequence to a breach of the duration limits (i.e. the "2+1+1" structure), fixed-term employment beyond the permitted term could carry a material risk of conversion to permanent employment term.

2 See MoM Regulation No. 19 of 2012 on Conditions for the Handover of Work to Other Companies, where there was an express distinction between a labour supply provision arrangement, and a service provision arrangement. Under the Job Creation Law framework, the concept of subcontract of work was no longer expressly included as a restricted arrangement. The Job Creation Law focused on restricting outsourcing or alih daya activities.

3 See Article 3 (1) of MoM regulation 7/2026.

2.3 Narrower grounds for termination

The Law sets out fifteen permitted grounds for termination of employment. Notably, termination on the ground of business efficiency (whether to pre-empt losses or in response to losses already incurred) is not among them. This marks a significant departure from the position under GR 35/2021, which recognises efficiency as a valid termination ground.

At the same time, the Law introduces an express ground permitting termination where the company closes as a result of the owner's decision to close permanently.

Notably, the previous regulatory regime merely imposed a broad requirement on employers to make efforts to avoid termination without prescribing specific measures. The Law now prescribes a sequence of measures, including reducing overtime, shifts, working hours or working days, not renewing expiring fixed-term contracts, adjusting managerial pay and facilities, temporary or rotating lay-offs, and voluntary early retirement before proposing to terminate employment relationships.

On its face, the Law appears to impose these measures as a general obligation applicable to all terminations. However, the nature of the prescribed measures suggests that they are only relevant where the termination is driven by business or cost considerations, and not where it arises from other circumstances, such as a corporate transaction or the sale of a business unit (for eg. reducing overtime would not be helpful to prevent a termination that is driven by the fact that the employee's role no longer exists due to a sale of business unit). It also remains to be seen whether, in financial losses scenarios, employers would be required to prove that each measure has been exhausted before termination or if adopting one of them would be sufficient. We expect these points to be clarified in the implementing regulations.

Interestingly, Article 228 paragraph (3) of the new Law provides for the statutory bipartite negotiations to be conducted with the labour union; direct negotiations with the employee are expressly contemplated where the employee is not a union member. This suggests that employers should involve the relevant union in the formal process rather than rely solely on individual negotiations with employees who are union members. We do not consider that this provision should be read as preventing all direct discussions with employees who are union members. However, the practical arrangements for union involvement and the scope for individual discussions alongside that process, may be clarified in the implementing regulations. Pending that clarification, employers should consider union involvement when planning proposed terminations involving union members, subject to the applicable statutory exceptions.

Without an efficiency-based termination ground, an employer facing declining profitability or seeking to streamline its workforce will generally have three options: (a) a closure supported by evidence of two consecutive years of continuous losses, which in practice is likely to require audited financial evidence; (b) a permanent closure of the business on the owner's decision; or (c) a termination by mutual agreement with the affected employee. For ongoing businesses, workforce reduction exercises driven by business considerations are likely to involve greater employee resistance and protracted negotiations.

2.4 Employment termination in the context of corporate transactions

The Law also removes a key qualifier for terminations in the context of corporate transactions. Under GR 35/2021, an employee could only decline to continue employment following an acquisition, and claim termination entitlements, where the acquisition resulted in changes to the terms of employment that were detrimental to the employee. The Law contains no such requirement. For any merger, consolidation, acquisition or spin-off, termination may occur where the employee is unwilling to continue the employment relationship, or the employer is unwilling to accept the employee, regardless of whether the employee's terms of employment are affected. In practice, this could mean that employees of a target company would be able to opt out following an acquisition and claim one times base severance and one times service pay even where their terms remain unchanged.

The Law does not define what any of these transactions (i.e. merger, consolidation, acquisition, or spinoff) mean, but we expect them to be read by reference to Law No. 40 of 2007 on Limited Liability Companies (as amended) and other relevant regulations.[4] Parties to corporate transactions should therefore factor potential employee opt-outs into deal timetables, pricing and the allocation of employee liabilities.

4 A merger and a consolidation involve the combination of companies into an existing or a new company, an acquisition is a takeover of shares resulting in a change of control of the company, and a spin-off involves the transfer of all or part of a company's assets and liabilities to one or more other companies.

2.5 Higher severance multipliers in certain scenarios

The Law increases severance entitlements for a number of termination scenarios, as summarised below:

Termination ground	GR 35/2021 (multiplier)	Law (multiplier)
Closure due to two continuous years of losses or force majeure (Article 237)	0.5x base severance + 1x service pay + rights compensation	1x base severance + 1x service pay + rights compensation
Force majeure (Article 239)	Closure: 0.5x + 1x + rights compensation. No closure: 0.75x +	1x + 1x + rights compensation
Closure on the owner's decision to close permanently (Article 238)	1x + 1x + rights compensation	1x + 1.5x + rights compensation
Suspension of debt payment obligations or bankruptcy (Article 240)	0.5x + 1x + rights compensation[5]	1x + 1x + rights compensation
Merger, consolidation, acquisition or spin-off with the worker unwilling to continue (Article 236(1))	Merger, consolidation or spin-off: 1x + 1x + rights compensation. Acquisition: 0.5x + 1x + rights compensation, and only where the acquisition resulted in detrimental changes to employment terms	1x + 1x + rights compensation, regardless of any change to employment terms
Merger, consolidation, acquisition or spin-off with the employer unwilling to accept the worker (Article 236(2))	1x + 1x + rights compensation	2x + 1x + rights compensation
Employer misconduct (Article 241(1))	1x + 1x + rights compensation	2x + 1x + rights compensation
Breach of employment terms by the employee (Article 244)	0.5x + 1x + rights compensation	1x + 1x + rights compensation
Retirement (Article 247)	1.75x + 1x + rights compensation	2x + 1x + rights compensation

On retirement payments, the Law permits specified employer-funded pension amounts to be taken into account, subject to its conditions, and requires the employer to meet any applicable shortfall. Mandatory old-age social security rights are also preserved.

2.6 New severance reserve funds

The Law requires employers to provide a severance reserve fund as a source of payment of employees' termination entitlements, managed by a government institution. The fund is intended to secure payment on terminations other than retirement for employees who are not enrolled in a pension programme. Micro and small businesses are exempt from this requirement. Non-compliance may result in administrative sanctions, ranging from a written warning to revocation of business licences. The contribution amount and mechanics will be set out in a Government Regulation, and the Law does not specify a compliance deadline so businesses should not assume that compliance may be deferred until 28 October 2027. As at the date of this bulletin, the government institution tasked with managing the fund has not been established. It also remains to be seen how the fund will operate in practice, including whether it will take the form of a pension-fund style arrangement with periodic employer contributions, how the contribution amounts will be determined, and what payment mechanism will apply.

2.7 Changes to minimum wage setting

The Law requires provincial Governors to set the provincial minimum wage by reference to decent living needs and economic and labour conditions, using either a formula based on economic growth, inflation and an index of between 0.5 and 1, or the decent living needs figure, with the higher value applying as agreed by the regional wage council. Provincial Governors must also set a

5 If the suspension of debt payment is not caused by company losses, the formula is 1x + 1x + rights compensation.

provincial sectoral minimum wage for certain lines of business and may also introduce regency/city sectoral minimum wages. Sectoral minimum wages apply to specified sectors, including leading sectors, sectors with distinct skills, characteristics or risks, and sectors involving heavier demands or specialisation. Sectoral minimum wages must be higher than the corresponding general minimum wage, although the Law does not prescribe a specific margin.

2.8 Enhanced leave entitlements

The Law significantly enhances statutory leave entitlements:

(i) **Long leave**: employees who have worked for five consecutive years (and every multiple of five years) are entitled to 30 calendar days of long leave, with no annual leave entitlement in that year if the long leave is taken. Under the previous Manpower Law, long leave was only available at certain companies as provided in the employment agreement, company regulations or collective labour agreement. It is now a mandatory entitlement for all employees.

(ii) **Annual and collective leave**: annual leave remains at a minimum of 12 working days, but if employers decide to apply Government-designated collective leave days (*cuti bersama*), these may no longer be deducted from annual leave.

(iii) **Maternity leave**: consistent with Law No. 4 of 2024 on Maternal and Child Welfare, maternity leave is extended to at least three months, extendable by up to a further three months for special conditions supported by a doctor's certificate.

(iv) **Paternity leave**: employees are now entitled to two days of paternity leave, extendable by up to three further days or as agreed, and two days in the event of a spouse's miscarriage.

2.9 Bipartite negotiation being a requirement

Previously, under GR 35/2021, bipartite negotiations were only required where the employee rejected the termination notice. Where the employee accepted the termination, no bipartite negotiation was required and the termination could proceed on the basis of mutual agreement.

The Law now requires all terminations to go through bipartite negotiations, with only four exceptions: resignation, expiry of a fixedterm contract, retirement, and the passing of the relevant employee. As termination by mutual agreement is not among these exceptions, bipartite negotiations appear to be required even where the employee does not dispute the termination. While the Law does not prescribe the form or mechanics of the negotiation, in practice, this is likely to require, at a minimum, minutes of the bipartite negotiation to be signed at the meeting where the employee signs the mutual separation agreement. Pending clarification in the implementing regulation, employers should build this into their termination process and practices.

2.10 Other notable provisions

Employers must continue to obtain an approved foreign manpower utilisation plan (RPTKA) before employing foreign workers. Its express exemptions cover diplomatic and consular employees, specified emergency production activities, business visits and research for specified periods, and foreign nationals who have been in a qualifying marriage to an Indonesian citizen for at least five years. In addition, employers must employ foreign workers who are willing to learn Indonesian to support technology and skills transfer, facilitate Indonesian language training (save for directors and commissioners, heads of representative offices, foundation organs and temporary work), appoint Indonesian counterpart workers and provide training. Foreign workers also remain prohibited from holding positions in personnel or human resources functions.

Separately, the threshold for mandatory establishment of a Bipartite Cooperation Institution (a forum for employers and employees to discuss and resolve work-related issues) is lowered from companies employing 50 or more workers to companies employing 10 or more workers.

The Law also provides separation pay for "specified termination reasons" as set out in the employment agreement, company regulations, or collective labour agreements. Where the company has not prescribed an amount, Article 233(2) provides that an amount of at least one month's wages may be determined.

Employers must also adopt a zero-tolerance policy on sexual harassment and violence, provide lactation facilities and ensure equal career development opportunities. An occupational health and safety management system is mandatory for companies with 100 or more workers or high-risk operations, and a health and safety committee must be established.

Finally, claims for wages and other employment-related payments may be brought without any time limit, and wilful non-payment of severance entitlements may attract imprisonment of up to four years.

3. What this means for businesses

(1) Review outsourcing and subcontracting arrangements

Companies should review their outsourcing practices, as outsourceable activities will be limited to the four supporting services under the Law. When subcontract of work is adopted, make sure that the arrangement fulfils the criteria set out in section 2.1 above (although unless the implementing regulations clarify otherwise, these measures are not risk-free). Mining, oil and gas groups and state-owned enterprises should also plan for any subsidiary restructuring required within the one-year transition period.

(2) Prepare for more limited termination options and higher severance exposure

Workforce reductions based on efficiency are no longer supported under the Law. A reduction will generally need to be based on a closure supported by two consecutive years of losses (which in practice is likely to require evidence, albeit not in any specific form pursuant to the Law), a permanent closure on the owner's decision, or the employee's agreement, and employers must document the prescribed prevention measures before commencing any termination process. Employers should anticipate greater employee resistance and protracted negotiations, and recalibrate their financial models for termination payment in light of the increased payment multipliers introduced by the Law, and budget for the severance reserve fund ahead of the implementing Government Regulation. In the context of an acquisition, employees may opt out and claim one times base severance and one times service pay, even where their terms remain unchanged.

(3) Review fixed-term employment arrangements and employment documentation

Employers should review fixed-term contract templates and existing fixed-term employment arrangements to ensure compliance with the new structure, notice and registration requirements. Company regulations and collective labour agreements should also be updated to align with the Law, including the new long leave, maternity and paternity leave entitlements, the treatment of collective leave, minimum separation pay and probation terms.

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