

South Korea: Case Study

The Policy Challenge

The Republic of Korea seeks to improve the productivity of enterprises, particularly small and medium enterprises (SMEs). One way it is doing so is by encouraging enterprises to have more training programs for their workers. To this end, the government has implemented a training levy rebate that requires enterprises of all sizes to pay training levies¹ as part of their employment insurance. The training levies are paid back in the form of rebates² to enterprises who train their workers voluntarily. The way it works is that enterprises pay for a training program for their workers, and then submit a claim to the government indicating the costs incurred. The government then pays enterprises back.

Results from the program show that much fewer SMEs apply for rebates than larger enterprises. Currently only 5% of SMEs are applying for the rebate and offering training programs to 4.2% of their workers. This means that most SMEs are paying for the levy but not benefiting from the rebate program or undertaking new training activities.

The Government of Korea is concerned. SMEs are the ones who need the most support in training activities but they are not benefiting from the current program. There are worries that the productivity gap between SMEs and large firms will continue to increase.

How can the policy intervention be re-designed to better serve SMEs?

Current Program Features

- **Policy Objective:** To create incentives for enterprises of all sizes to undertake voluntary worker training programs that improve their productivity.
- All enterprises are charged the same upfront training levy of 1 million won (\$1,000 USD) per year, regardless of whether or not they implement any training programs.
- SMEs can claim training rebates up to 2.5 million won (\$2,200 USD) compared to a maximum of 1 million won (\$875 USD) for large firms. This gives SMEs a higher incentive to participate, because they can gain more money back in rebates than the original levies they paid.
- The program favours formal institutional training over on-the-job training by offering twice the rebate for formal training compared to in-plant training.
- Training costs are paid upfront by enterprises and rebates are provided after the training has been completed and approved through a government application process.

Questions

1. **Why do you think that SMEs are not applying for the rebate? List the possible reasons that SMEs would not participate in the training incentive program.**
2. **How would you re-design the policy intervention to address these challenges and increase the participation and benefits to SMEs?**

¹ Training levies are upfront fees the government charges to enterprises of all sizes regardless of whether or not they implement training programs.

² Training rebates are funds the government repays to those enterprises who offer training programs to their workers. The money for rebates comes from the levies collected upfront.

Hints:

- Think of an SME that you know well and list any barriers or reasons they might give you for not applying or participating in the rebate. Take these into consideration when designing your policy intervention.
- Consider possible partnerships that could be created. What could be the different roles for government, associations, the private sector, training service providers, universities etc.?

Areas to Consider:

In designing your policy intervention, consider improvements to any of the following areas:

1. Outreach and promotion of the program to SMEs
2. Identification of SMEs' training needs
3. Mechanisms for cost sharing between SMEs
4. Human Resource needs for coordinating trainings
5. Balance of institutional training vs. on-the-job training
6. Application process to claim the rebate from government
7. Timing of the rebate repayment (currently issued after training is completed)
8. New partnership models with other actors

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Additional Information

- Recent data shows SMEs account for 99% of all enterprises, 88% of employment, and 50% of both total output and exports in Korea (2014).
- One of the most common productivity barriers raised by SMEs in Korea is the challenge of securing technical and skilled workers.
- To respond, the Ministry of Labour introduced the training levy rebate system that requires enterprises of all sizes to pay training levies as part of their employment insurance.
- The training levy was applied on 7 million employees. SMEs represented 65% of these employees, but only 5% of SMEs applied for the levy rebate covering training programs for 4.2% of their workers.
- In comparison, 78% of large firms applied for the levy rebate covering training for 38% of their workers.

Common Barriers

The following summarizes some of the common barriers that SMEs face:

- **Information:** SMEs often do not have the same access to information and knowledge as large firms. As a result, many SMEs are unable to accurately identify their workers' training needs. They may also be unfamiliar with training services that are available in the market. Often SMEs do not access government programs because they do not know the programs exist, do not understand the benefits to SMEs, or are unclear on the steps of how to apply and participate.
- **Administrative:** Most SMEs do not have a dedicated Human Resource staff to oversee training programs for their workers. This differs from large firms, who often have dedicated staff in-house to manage their training needs. The role of this staff is to identify the training needs of workers, find suitable training service providers, negotiate training rates, and monitor the results. This staff would also be responsible for filling out administrative documents to submit a claim to government for the training rebate. The rebate rates are not high enough to cover the costs of SMEs hiring more Human Resource staff.
- **Organization Size:** Given that SMEs have less workers, their participation in training programs usually means a disruption in production, which comes at a financial cost. The cost of training per worker is also higher than in large firms, because SMEs are training less workers per session. Workers in SMEs tend to stay with their employers for shorter periods of time, meaning there is a high risk of poaching³ by other companies, especially if workers participate in institutional trainings that take place outside of the firm.
- **Financial:** SMEs have much more difficulty accessing credit than larger firms. Banks generally consider SMEs to be a greater risk and therefore charge higher interest rates or decline access to credit altogether. SMEs also have limited cash flow, making it more difficult to pay for training fees or other lump sum payments.

³ Poaching refers to the practice of companies hiring employees from their competitors. Employees with specialized skills are particularly targeted by competitors who can offer higher salaries and benefits.