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REVIEW OF LABOUR MARKET AND SOCIAL SAFETY-NET POLICIES IN KOREA

(Note by the Secretariat)

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Introduction

Until the 1997 financial crisis, Korea exhibited one of the most impressive economic records of modern capitalism. In 1953, the country emerged from the ashes of the Korean War as one of the poorest in the world. It followed several decades of rapid economic development, as amply documented in many studies, and, in 1996, Korea became a member of the OECD.

With the advent of the financial crisis, the impressive economic development process came to a sudden halt. The crisis hit many workers and their families hard, in a country where the social safety-net was not as firmly established as in other OECD countries.

However, the economy has now turned the corner. GDP has grown vigorously over the past few quarters and the prospects are for a continuation of the solid recovery underway. The recovery owes much to supportive macroeconomic policies, including the substantial devaluation of the won that occurred at the beginning of the crisis. However, the implementation of structural reforms, including in the area of labour and social policies, has also played an essential part in the recovery.

The fact that a solid recovery is now underway should not lead to any let up in the reform process and the purpose of this Review is to identify those areas where labour market and social safety-net policies could be further strengthened. The Review begins with a summary of the main findings and policy conclusions. It then provides an overview of the Korean labour market and an analysis of the main employment and social challenges that lie ahead (Chapter 1). The extent to which different policies can address these challenges is then reviewed in the following chapters, namely the complex issue of labour law and industrial relations' reforms (Chapter 2), labour market programmes and the public employment service (Chapter 3), and social assistance policies (Chapter 4).

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Summary and Policy Conclusions

Korea was a star economic performer before the crisis.

Korea has experienced one of the most impressive economic records of modern capitalism. Following the Korean War, from which the country emerged as one of the poorest in the world, the economy registered four decades of almost uninterrupted rapid growth. Today, per capita income has reached 60 per cent of the OECD average (close to the levels in Greece and Portugal), while Korea has earned an international reputation as a successful exporter of technologically-advanced goods, such as micro-chips and electronic equipment.

The economy has recovered from the crisis quickly,...

The financial crisis which started at the end of 1997 brought the growth process to a sudden, unexpected halt. The crisis forced the government to agree to a rescue package with the IMF. Unemployment rocketed from 2½ per cent to a peak of 8½ per cent in early 1999, and more than one million Koreans were thrown into poverty. The difficult economic and social situation forced the authorities to implement quickly a wide range of macroeconomic and structural reforms, notably in the areas of labour market policies and social safety-nets. In response to these reforms, the economy has now turned the corner, permitting the unemployment rate to fall rapidly to about 5 per cent, and short-term prospects point to a continuation of the solid recovery.

... but the Review argues that much remains to be done.

In this context, it may be tempting to assume that the crisis was just a blip in an otherwise high-growth path and that, as a consequence, there should be a pause in the reform agenda. On the contrary, while it pays due tribute to what the Korean authorities have achieved in a very short period of time, this Review argues that much remains to be done to strengthen the social sustainability of the development process. It calls for further actions to consolidate the industrial relations' system, reform labour law, and to improve the coverage and effectiveness of labour market and social safety-net policies. The recovery should not lead to any let up in these policy reforms.

The role of labour and social policy in the recovery

Recovery from the crisis has been facilitated by agreements between the social partners,...

The Tripartite Commission has been instrumental in achieving agreement between the social partners and the government on the response to the crisis. Thus, the Tripartite Commission's agreement of February 1998 urged the major industrial conglomerates (*chaebols*) to improve the effectiveness and accountability of corporate governance and introduce greater transparency of their management and accounts. In addition, the agreement recommended a substantial reduction in the indebtedness of the *chaebols*. In order to facilitate enterprise restructuring, it was also decided to make it legally possible for firms to dismiss workers

for “urgent managerial reasons”, and greater flexibility was introduced in the area of temporary work through the legalisation of agencies for so-called “dispatched workers”.

... substantial wage moderation, and...

In addition, wage moderation has been substantial. In 1998, average nominal wages per employee fell by 2½ per cent, equivalent to a cut by almost 10 per cent in real terms (which is unusually large by OECD standards), cushioning the effects of the crisis on unemployment. Such wage moderation was mainly attributable to the dramatic cut in bonuses and overtime payments, which account for a significant portion of Korean wages and are mainly determined by firms’ economic performance. In 1999, as a result of increased overtime and bonus payments, wages rose robustly (by over 10 per cent in real terms), so recuperating their pre-crisis level in real terms. However, since in the meantime labour productivity has increased (by about 6 per cent, cumulatively, in 1998-99), real unit labour costs have been reduced, thereby improving business profitability and providing room for reducing corporate indebtedness. Together with the depreciation of the won in 1998, these wage and productivity trends have enhanced the cost-competitiveness of the Korean economy, contributing to an export-led recovery.

... the strengthening of labour market and social safety-net programmes.

Also, a wide range of labour market programmes was either strengthened or introduced since the start of the crisis, and this has helped provide a degree of social insurance for job losers and their families and maintain the employability of many individuals who otherwise might have lost contact with the labour market. Reflecting these efforts, government expenditures on labour market programmes increased from negligible levels in 1997 to 2¼ per cent of GDP in 1998 and 3¼ per cent in 1999. Finally, an effort has been made to provide modest social assistance support to those who have fallen out of the social safety-net, thereby alleviating social hardship and making the much-needed structural reforms socially sustainable.

Remaining challenges

Significant challenges remain, however, notably as regards industrial relations,...

However, the Korean economy still faces several major labour market and social policy challenges as it seeks to consolidate the recovery and the social sustainability of its development process. First, it is more necessary than ever to create a less confrontational and more consensual system of industrial relations if the Korean economy and society is to modernise and prosper. Unfortunately, past confrontational attitudes between the social partners have re-surfaced in a context of economic recovery. The result is that consensus on wage moderation and reforms of employment conditions and workforce practices is increasingly difficult to achieve.

... the level of unemployment and non-employment,...

Second, joblessness remains a problem. True, open unemployment is low by international comparison but, unlike the case of many other OECD countries, the majority of unemployed workers do not receive any unemployment benefits. In addition, the degree of labour market slack is significantly higher than suggested by the open unemployment rate, as

indicated by the high number of discouraged workers (the total participation rate is 1.7 percentage points lower than in 1997) and of participants in labour market programmes such as public works. Importantly, the youth (especially those with high-school education) are disproportionately affected by unemployment, suggesting that school-to-work transition is difficult in Korea.

... the high degree of job precariousness,...

Third, jobs tend to be much more precarious in Korea than is the case in most other OECD countries. Only 30 per cent of employed workers have a “regular” (i.e. permanent) contract, which is the lowest figure in the OECD area, followed by Turkey. One third of the employed have a temporary or daily job. As a result, job tenure in Korea is low by international comparison -- on average, workers stay with the same employer about six years, compared with over 11 years in Japan and 7½ years in the United States. Importantly, the incidence of non-regular jobs in small businesses and among women is very high. As the recovery gets firmly established, the expectation is that employers will become more confident about the economic prospects and that, as a result, they will be less reluctant to convert non-regular jobs into regular ones. However, it should be stressed that the incidence of regular employment did not increase much in 1990-97, a period characterised by near-full employment. Job precariousness indeed seems to be a structural characteristic of the Korean economy, which is problematic not only from the social point of view, but also for reasons of economic efficiency. Indeed, job precariousness seems to be associated with a relatively low incidence of vocational training (in particular in small businesses), in turn inhibiting productivity growth.

... widening income inequalities,...

Fourth, income inequalities have started to widen. Over the past three years, average incomes of the poorest 20 per cent of households have declined by over 8 per cent, while average incomes of the richest 20 per cent of households have increased somewhat.

... rising poverty, and...

Fifth, a large number of households live with very low incomes. In 1999, 8 to 12 per cent of Koreans (depending on the source) were officially estimated to live in poverty -- based on a minimum monthly cost of living representing the equivalent of 350\$ (in purchasing power parity terms). Job-losers, the elderly and lone-parent households are disproportionately affected by poverty. The extended family has long provided an effective source of income support in Korea -- the so-called “Confucian social welfare system”. However, the supportive role of the extended family has weakened in recent years.

... surprisingly weak multi-factor productivity gains.

Finally, the productivity of the Korean economy is a matter of concern. Past economic growth performance rested on a formidable investment effort: during the 1990-97 period, the share of national income devoted to real fixed capital accumulation averaged 37 per cent, a very high figure by international comparison. The returns from some of these investments, however, have turned out to be very small or even negative -- one of the underlying factors behind the 1997 crisis. Reflecting the poor returns from many investment projects, multi-factor productivity (a measure of overall

economic efficiency) stagnated over the period 1990-97, while it grew in nearly all other OECD countries. Clearly, in order to strengthen the growth process in the future, it is essential that resources are used more productively than hitherto.

Addressing these challenges requires an improvement in the coverage and efficiency of labour market and social safety-net programmes, while also making further progress in bringing industrial relations and labour laws into line with internationally-agreed standards.

Policies to address the key challenges

Freedom-of-association and collective bargaining rights

Addressing these key challenges requires, first, a consolidation of freedom-of-association and collective bargaining rights.

It is useful to recall the context under which the issue of freedom-of-association rights has been discussed in the OECD. Aware of concerns regarding these rights, the OECD Council, when inviting Korea to join the organisation in October 1996, welcomed the commitments made by the Korean authorities “to reform existing laws on industrial relations in line with internationally accepted standards, including those concerning basic rights such as freedom of association and collective bargaining”. The Council also instructed the ELSA Committee to “monitor closely the progress made on labour law reforms in the light of that commitment”. In discussions on these issues in the Council, the ELSA Committee and other international fora (notably at the International Labour Organisation and its Committee on Freedom of Association), attention has centred on a number of areas where Korean law and practice in industrial relations was believed to be in conflict with internationally-accepted standards. These include issues of trade union pluralism, third-party intervention in collective bargaining, the right to organise of public servants and teachers, the right to strike in the public sector, trade union membership of dismissed or unemployed workers and the payment by companies of their full-time trade union officials. Concerns have also been voiced in these fora about the arrest and imprisonment of trade unionists for activities that would be regarded as pursuit of legitimate trade union goals in other Member countries.

The situation regarding these rights has improved,...

Since the start of the monitoring process, there is no doubt that the legislative reforms have shifted Korean labour laws significantly in the desired direction. Major examples include the recognition of the principle of trade union pluralism, the legalisation of teachers’ unions, freedom for many civil servants to engage in workplace associations, the gradual reduction of the list of so-called “essential services” where compulsory arbitration applies, as well as the recent recognition of the KCTU as the second national trade union centre. In addition, the government has decided to allow from 2002 on trade union pluralism at the enterprise level.

... but more needs to be done on the legal

However, there are some outstanding issues and resolving them would probably contribute to create a climate of trust between the social partners.

front,...

First, civil servants are not allowed to join trade unions and bargain collectively. *Second*, trade unions face legal and practical impediments in deciding who to accept as members. *Third*, the law will, as of 2002, prohibit the payment of full-time union officials. On these three issues, the government, in consultation with social partners, should explore avenues for amending the relevant provisions of the law. Finally, over the past few years, waves of militant trade union action and subsequent arrests of trade unionists have succeeded each other. It will thus be particularly important for the Korean authorities to take all the necessary steps to avoid large-scale arrests and detentions of trade unionists engaged in pursuit of union activities. In particular, legal provisions, which often lead to the arrest of trade unionists for what other OECD countries consider legitimate trade union activities, need to be revised or used with utmost restraint.

... and also to improve the industrial relations climate.

Finally, alongside further progress on the legislative front, concern remains about the present climate of industrial relations in Korea at both the national and enterprise levels. The repeated withdrawals by both labour and business representatives from the Tripartite Commission and the lack of any agreed agenda and timetable for its discussions are disturbing. In order to foster social dialogue and mutual trust in the Tripartite Commission, the government could take the lead by presenting reform proposals for discussion in the commission. Needless to say, the government should also make appropriate efforts to act upon compromises reached within the Commission (as required by the 1999 Tripartite Commission Act), while the social partners need to recognise the futility of “empty chair” attitudes and come forward themselves with constructive proposals rather than always looking to the government to solve deadlocks. Perhaps more importantly from the point of view of Korean productivity performance, tripartite agreements at the national level need to be supplemented by active labour-management consultation and effective co-operation at the enterprise level.

Labour regulations and public pensions

Second, to the extent that the public pension system is made sustainable, lay-off provisions could be revised,...

While the new lay-off provisions are clearly a step in the direction of increasing numerical flexibility in firms, “regular” workers still enjoy a relatively high degree of employment protection compared with their counterparts in other OECD countries. While the one-month notice period, even for workers with high tenure, is low by international standards, the legal severance pay requirements applying to regular workers would seem to be relatively onerous. In addition, the preconditions for dismissals based on economic reasons (advance notification to a trade union, verifiable efforts to avoid dismissal, etc.) make conditions in Korea resemble closely those in other high-protection countries such as Japan, Portugal, France or Germany. Finally, the new provisions on notification of collective dismissals to the Ministry of Labour correspond to the strict regulations in force in EU countries. Overall, the OECD has ranked Korea as the second strictest country out of 27 member countries in terms of protection of regular (or permanent) employment contracts. There would therefore seem to be room for easing the legal severance pay requirements for regular

workers. This reform, however, should take place gradually, and be dependent on *a*) the Employment Insurance System (EIS) becoming more firmly established in coming years (see below); and *b*) the public pension system being adequately funded, which is far from being the case at present.

... and this would contribute to reduce job precariousness.

Relaxing relatively strict employment protection for regular workers, under the above conditions, could also help ease job instability for temporary and daily workers (who form the core of “outsiders” in Korea). This would hopefully encourage employers to convert more non-regular contracts into regular ones, thereby reducing the degree of labour market segmentation, which is presently very pronounced, and laying the ground for greater investment in on-the-job training. In addition, the social and legal protection of fixed-term and daily workers should be enhanced.

Labour market programmes and the public employment service

Labour market programmes have to be evaluated in the light of their twin objectives, namely *a*) to provide income support to the unemployed; and *b*) to foster the future employment and earnings prospects of unemployed workers, while minimising the dead-weight, substitution and displacements effects often associated with such policies.

Third, the coverage of the Employment Insurance System needs to be expanded urgently,...

Regarding the first objective, the portfolio of labour market programmes has been expanded considerably in the past two years. However, official estimates show that only one in eight of the unemployed receive unemployment benefits (in addition, less than half participate in some type of labour market programme, the others being potential clients for social assistance benefits). It has recently been decided to expand the scope of the EIS to cover daily workers, but there remain serious implementation problems, in particular among small firms which often evade the payment of social contributions. The current situation is not satisfactory and the government should assign a high priority to increasing the coverage of the EIS and make sure that vulnerable groups are not left unprotected, as is presently the case.

... the effectiveness of active labour market programmes should be enhanced, and...

As to the labour market effects of labour market programmes, it is not possible to draw clear-cut conclusions in the absence of any systematic evaluations. However, based on the examination of specific design features of the programmes, the following observations can be made:

- there is a general lack of targeting in many of the programmes. As a result, it is unclear whether they really reach disadvantaged groups, such as unemployed workers not covered by the EIS and young unemployed workers. Targeting is especially important in the case of subsidies to SMEs, given that this programme is the largest in terms of government spending on active labour market programmes (ALMPs);
- despite a general lack of targeting, some of the programmes are not much used. This suggests that some regrouping of programmes may be

called for, notably in the area of employment maintenance subsidies;

- now that a brisk recovery is underway, there is a strong case for scaling back substantially public works programmes. International evidence suggests that these programmes, unless they are well targeted on hard-to-place groups, are particularly susceptible to large dead-weight losses;
- there may be cases where work does not pay -- leading to a risk that some benefit recipients may prefer to stay in the programme rather than look actively for a private-sector job. For instance, remuneration in public works programmes reportedly competes with market wages in certain unskilled occupations;
- training institutions have had difficulties in coping with the rapid and massive expansion of training programmes. In addition, the type of training provided by some of them may not be closely tied to the requirements of a complex, modern economy such as Korea. For these reasons, there is a good case for a greater involvement of social partners at the local industry level in programme design, while also expanding the training capacity; and
- the outcomes of the programmes should be carefully monitored and evaluated.

... the public employment service should be rationalised,...

Finally, the role of the public employment service (PES) in the design and implementation of ALMPs could be enhanced. The concept of the “one-stop office” is a good one, and should be generalised by integrating the separate networks of Employment Security Centres and Manpower Banks. Also, while it may have been useful in the period of rising unemployment to operate another chain of placement offices under the authority of municipalities and other local governments, the co-existence of two types of “public employment services”, one under the Labour Ministry and the other under local government, that are involved in the same types of tasks (apart from benefit payment), may not prove efficient in the long run.

... the quality of its staff upgraded, and...

As mass unemployment declines, PES officers will need to devote more efforts to counselling and monitoring of those job-seekers who are at high risk of long-term unemployment and benefit dependency - at present there is little “profiling”. Needless to say, the efficiency of the PES crucially depends on the quality of its staff and the high turnover of counsellors is problematic in this respect. In present circumstances, improving training and job stability of the staff might be more important than increasing the number of officers. The steep decline in unemployment should provide the necessary breathing space to concentrate on improving the quality of PES staff.

... opportunities be taken to strengthen complementarities with private employment

In addition, Korea should seek to take advantage of the extensive network of private employment agencies that presently exist. These agencies have an excellent intermediation record in the unskilled labour market and the PES could seek complementarities with them, for example

agencies.

by contracting out the placement of low-educated unemployed.

Social assistance programmes

Fourth, there is a need to introduce an effective social assistance programme.

After the crisis, given the relatively low coverage of unemployment benefits and other labour market programmes, demand for social assistance benefits increased dramatically. The authorities responded by expanding the existing programme and creating a new one, specifically targeted on low-income individuals of working age. In 1999, nearly 2 million individuals received social assistance benefits. This, however, represents only 55 per cent of the estimated number of persons living in poverty in that year.

The new law seeks to expand coverage on a “productive welfare” basis,...

The weaknesses of the present social assistance system have prompted the Korean authorities to enact a new system, namely the National Basic Livelihood Security Law (NBLS), to take effect as from 1 October 2000. The concept underlying the new social assistance law is that of “productive welfare”, *i.e.* the purpose is to provide adequate income support while also encouraging benefit recipients to participate in the labour market. Thus, it is officially estimated that the proportion of individuals living in poverty that will receive benefits will be increased to two thirds after the new law comes into force. In addition, the level of benefits will be raised.

... but, despite the good intentions, benefits will remain low and many needy individuals will not be covered...

However, it is important to stress that many low-income individuals will remain unprotected under the NBLS. This might reflect the fact that benefit entitlement is subject to unusually strict income criteria, based on the income capacity (and not actual income) of the extended family. This particular provision of the law may have to be revised, if the official target of providing benefits of last resort to those in need is to be reached. Also, despite their increase, benefits will remain very modest. The authorities should consider raising them, perhaps in stages, so that they reach at least the poverty line.

... and the incentives to improve job prospects of recipients can be improved in various ways.

In addition, making productive welfare a reality requires local government officers responsible for the delivery and administration of the system to screen recipients on their work ability and provide employment-oriented counselling services. Based on the experience of other OECD countries, it is possible to identify certain policy avenues which could help meet these goals:

- at present, there are about 250 recipients to each welfare officer, compared with an OECD norm of 80 to 120 recipients per officer. Korean welfare officers simply do not have the time to screen and adjudicate clients on their work-ability or provide intensive job-counselling services. The authorities have undertaken to hire additional welfare officers so that the number of recipients per welfare officer declines to 200, but many more would need to be hired and trained;
- welfare officers will require adequate funds to provide job-counselling or, in certain cases, offer social assistance recipients the possibility to

attend training courses. In this regard, the authorities could consider the implementation of pilot projects, allowing private agencies to tender for the provision of employment services to NBLs clients. In such a system, the issue arises of whether able-bodied recipients of working age would lose their benefits in case they refuse a job offer or a training course;

- to encourage job search, it may be helpful to introduce in the NBLs a mechanism of earnings disregards which permits recipients to keep their benefits while at the same time earning an income, up to a certain threshold. Such a system would have to be rather different from the one embodied in the current setup.

Financing arrangements could be improved by reducing distorted incentives between central and local governments.

Current financial arrangements between different levels of government may be conducive to a waste of resources. At present, most of the budget for social assistance benefits comes from central government, while local governments (and their welfare officers) are in charge of the delivery of benefits. In such a setting, local governments have a weak incentive to enforce the different eligibility criteria and they might therefore be inclined to provide benefits to whoever asks for them. Up to now, the central government has addressed this problem by announcing strict budget limits, effectively imposing hard-budget constraints on local governments. But, under the NBLs, the plan is to provide social assistance benefits as of right. Even so, it seems desirable to maintain the current budgetary “grant-based” system and not give the certainty to local governments that their financial demands will always be satisfied.

Education and training

Fifth, the quality of education and training needs to be enhanced.

Finally, the average educational attainment of the Korean population and work force has increased spectacularly over the past decades, contributing to the rapid growth performance. Practically one fifth of the total Korean population has a college degree, the highest figure in the OECD after the United States and the Netherlands. However, there is a need for improving the quality and relevance of education and training, in order to raise multi-factor productivity and allow Korean firms to compete effectively in the 21st century.

Financing of programmes

There is room for financing the expansion of much-needed programmes.

Some of the measures advocated above will exert upward pressures on government spending, raising the issue of how they can be financed. In the case of an expansion of the EIS, extending the coverage of benefits to workers of small enterprises, which often do not pay the social contributions, risks creating a deficit in the EIS. In order to prevent this, it is essential that the government step up its efforts to make all firms pay their social contributions. Otherwise, the government may face pressures for subsidising the EIS, a practice that would be both unfair and inefficient. In the case of programmes financed by central government, notably social

assistance benefits for which an expansion is also planned, resources can be found by scaling down programmes such as public works and unemployment loans. Further savings could materialise if rigorous evaluations of ALMPs were carried out, thereby reducing the risk of waste of existing resources. Should these savings prove insufficient, the government could consider raising tax revenues. Preferably, this should be done by enlarging the tax base (through an intensified campaign against tax evasion) rather than raising tax rates which, at between 10 and 40 per cent, are not particularly low by OECD standards. In any case, general government revenues represent about 25 per cent of GDP which is, after Mexico, the lowest figure among OECD countries for which comparable data exist.

Concluding remarks

There should be no let up in the momentum of reforms.

In sum, despite the recovery, now is not the time to reduce the momentum of reforms. Korea has managed to catch-up rapidly vis-à-vis other OECD countries, but further progress may be more difficult than is often thought. Indeed, future improvements in living standards may have to rest on using resources more efficiently, rather than more intensively as was the case before the 1997 crisis. A more qualitative approach to the development strategy may be called for, encompassing an increased emphasis on enterprise training, a reduced labour-market duality and the establishment of a well-functioning social safety-net that covers all individuals. It is particularly urgent to *a)* improve the quality of education and foster enterprise training, *b)* expand the coverage of both the EIS and social assistance benefits, while scaling back programmes adopted as a temporary response to the crisis, *c)* improve the financial sustainability of the public pension system, which, if successful, would permit a gradual reduction of enterprise retirement allowances for regular workers, thereby reducing the marked duality that presently exists and laying the ground for higher productivity gains, *d)* better target ALMPs, enhance the quality of the PES staff and undertake rigorous evaluations of the programmes, and *e)* make sure that work continues to pay in Korea.

Obviously, these measures need to be adopted in a context of full respect for basic workers' rights and, in this sense, resolving remaining industrial relations' issues should rank high in the policy agenda. In a modern, productive economy, it is important that all social actors be involved in the reform process in a climate of mutual respect and trust.

CHAPTER 1 THE LABOUR MARKET

A. Introduction

1. Over the past three decades, the Korean economy developed at a remarkably fast rate and the country came to be known as one of the Asian “tigers”. This high-growth period was characterised by substantial increases in investment in physical and human capital, rapidly rising real wages and declining income inequalities. However, the economy was hit heavily in 1997 by the financial crisis that swept through much of Asia. The crisis brought in its wake dramatic labour and social consequences. However, it did not last long: by the second half of 1999 the economy was already recovering strongly.

2. This Chapter attempts to provide a synthetic overview of the labour market of Korea that embraces the 1997 economic crisis and the ongoing economic recovery. Next, the current challenges of the labour market are highlighted. In particular, an attempt is made to identify labour market imbalances that may require further policy action.

B. Economic development, the financial crisis and the labour market

3. The first stages of economic development in Korea were characterised by heavy government intervention.¹ After the end of the Korean War and the partition in two countries, economic policy focused on import substitution. The 1960s saw a policy shift toward an export promotion strategy, characterised by high rates of investment in human and physical capital. From the seventies to date, educational attainment has increased considerably (see Chart 1.1). The number of lower-educated men fell from over 60 per cent of the population in 1970 to almost 18 per cent in 1995; for women, the corresponding figure went down from 85 per cent to 35 per cent. This strategy laid the basis for high economic growth. Most raw materials were imported, as the economy lacked natural resources. A small number of large conglomerates, the *chaebols*², emerged as key engines of development, while at the same time acquiring considerable economic and political power. By the 1990s, high-technology and service industries were able to compete with industries of more developed economies.

4. During most of the past three decades, output and employment grew steadily and rapidly, although for a long time this did not lead to a situation of overheating as there was ample rural labour supply available.³ High real wage increases⁴ were accompanied by strong labour productivity gains,

1. See Corbo and Suh (1992), Chapter 2, for more details.

2. Until recently, the largest ten *chaebols* were Hyundai, Daewoo, Samsung, LG (Lucky-Goldstar), Sunkyong, Hanjin, Ssangyong, Kia, Hanhwa and Lotte.

3. Output fell in 1980, for the first time since the start of the development process.

4. The same pattern of fast increasing wages and GDP holds also in the case of the tigers of Taiwan and Hong Kong (Fields, 1994).

although this is not the case in terms of multi-factor productivity, as shown below (Corbo and Suh, 1992; Fields, 1994; Kim and Topel, 1995). Unemployment rates reached very low levels throughout the 1980s and 1990s, averaging less than 3 per cent for men and less than 2 per cent for women.⁵ As the labour force became more educated, a shortage of unskilled labour slowly emerged, which was filled up mainly with foreign labour. For example, over 13 per cent of vacancies for unskilled workers remained unfilled in 1996, against an average number of unfilled vacancies for all skills of 3 per cent in the same year (Park, 2000).

How the 1997 financial crisis hit the labour market

5. Korean financial markets were severely hit in 1997 by a crisis that was sweeping throughout Asia. The economy was caught by surprise. Ex-post, the low profitability and high debt levels of the corporate sector together with the poor functioning of the financial system and the large size of short-term foreign debt relative to the size of international reserves were identified as weaknesses that exposed the country to the crisis (OECD, 1999f). In December 1997, the government negotiated a financial support programme with the IMF. Though financial markets started to stabilise in early 1998, GDP dropped by 5.8 per cent (Table 1.1).

6. The labour market was especially shaken by the crisis, in marked contrast with the near full employment situation prevailing during 1990-97:

- Many Koreans lost their jobs and unemployment rose to 6.8 per cent in 1998 before peaking at 8.6 per cent in February 1999 (Table 1.2). The number of the unemployed went up from 0.5 million before the crisis to 1.5 million in 1998, before reaching 1.8 million in February 1999. The job cuts hit mostly low-skilled workers (Park, 1999). The real degree of labour market slack is even more pronounced if discouraged workers are taken into account (Box 1.1). Unemployment was a shocking new experience for many Korean workers and their families.
- The participation rate fell by 1½ percentage points in 1998, and by a total of nearly 5 percentage points in less than two years (Table 1.2). Especially pronounced was the fall in participation rates for women and youth aged 20 to 24.
- Total employment decreased from 21.1 million in 1997 to 19.9 million in 1998 before falling further to 19 million in the first quarter of 1999, registering a decrease of almost 10 per cent in less than two years (Shin, 1999). During 1998, employment in agriculture grew slightly for the first time since the late seventies, as some women went back to the countryside; the number of women employed as unpaid family workers increased by 6 per cent in 1998.

7. Nominal and real wages fell dramatically from 1997 to 1998, by 2½ per cent and 9.3 per cent, respectively (Chart 1.2). Nominal wage cuts are mainly attributable to a reduction in overtime payments and bonuses (by 15 per cent and 17 per cent, respectively). By contrast, the basic wage recorded a small increase of 3.7 per cent, which still represents a fall of 3½ per cent in real terms. The response of wages to the crisis shows a flexibility that finds no equal in other OECD countries. This is to some extent due to the structure of wages in Korea, which are partly determined by pay elements that depend on enterprise performance. But moderation in collective agreements has also played a key role. Large firms reduced wages less than smaller ones and the largest wage cuts were experienced in the construction sector. Also wages of civil servants were cut by about 10 per cent. In addition, 16 per cent of all job-lossers reported that

5. Although the measurement of unemployment in Korea does not correspond closely to the OECD guidelines, this is unlikely to have had a large impact on these statistics (see Box 1.1 for a discussion).

they had experienced problems of wage arrears and 27 per cent of the older workers who had lost their job reported that they had not been paid all or part of their redundancy pay entitlement (Park, Y.B., 1999).

8. The combination of lower earnings and job losses had dramatic consequences on household incomes. Income inequality increased in the aftermath of the crisis (Fields, 1999; Kakwani and Hyun, 1999; Park, Y.B., 1999). For urban workers, the shares of income of the first 9 deciles of the income distribution fell and the Gini coefficient of income inequality rose from 0.28 in the last quarter of 1997 to 0.32 in the first three-quarters of 1998 (Moon *et al.*, 1999). Increases in poverty are discussed in Chapter 4.

9. The government reacted promptly to the unprecedented rise in unemployment. A budget for public works and training programmes for the unemployed was set up quickly. Entitlement to unemployment benefits was progressively expanded and the duration of payments extended (see Chapter 3). Social assistance benefits were granted temporarily to the unemployed that had no other source of income (see Chapter 4). The rapid policy response reflects the gravity of the crisis but also, more fundamentally, the centralised decision-making set-up for labour market and social safety-net policies (see Annex A).

Box 1.1 The measurement of unemployment

Unemployment is measured on the basis of information drawn from the survey of the “Economically Active Population”, which is carried out by the National Statistical Offices of Korea on a monthly basis since July 1992. The survey sample refers to the resident population aged over 15. Foreigners, those in prison and the military are not covered by this survey. The unemployed are defined as those persons that are not working but are available for work and actively seeking work during the reference week. All individuals that worked over one hour for pay, or over 18 hours in the case of unpaid labour, or that were employed although out of work temporarily because of holidays or sick leave, in the reference week, are counted as employed.

Unemployment in Korea, based on the above definitions, is not directly comparable with unemployment in other OECD countries, as measured by the standardised unemployment rate (SUR). According to the SUR methodology, the armed forces are counted as employed, while foreigners, either employed or unemployed, are considered as labour force participants. Finally, the reference period for job search according to the SUR is four weeks, rather than one week as in Korean practice.

It is difficult to say *a priori* whether the Korean rate of unemployment would be higher or lower if measured according to the SUR methodology. Counting the armed forces and foreign labour as part of the employed would drive down the unemployment rate; in 1997, there were 690 000 individuals in the army and about 250 000 foreign workers, according to official sources. On the other hand, defining the job-search requirement over four weeks, rather than one, is likely to raise the number of the unemployed. Since they joined the OECD in 1996, the Korean authorities have started to adapt their statistical practices. Recent estimates suggest that, in September 1999, the Korean SUR would be 5.1 per cent, compared with 4.8 per cent under current definitions.

Finally, it has been argued that official statistics on unemployment tend to underestimate the extent of labour market slack in Korea, as many unemployed persons who cannot find a job within a short period of time report themselves as non-participants. This is due to the fact that in the face of the crisis, job-losers and new entrants to the labour market have tended to withdraw from the labour market -- the “discouraged worker” effect. Some estimates are provided in the table below.

**Official unemployment rate
and unemployment rate including discouraged workers by sex**

	Official unemployment rate ^a			Unemployment rate including discouraged workers ^b		
	Total	Male	Female	Total	Male	Female
1995	2	2.3	1.7	3	2.8	3.3
1996	2	2.3	1.6	2.9	2.9	3.1
1997	2.6	2.8	2.3	4.1	3.6	4.8
1998	6.8	7.7	5.6	9.9	9.3	10.8

a) National Statistical Office (NSO) b) Kim and Moon (1999)

1. The recovery already under way in 1999

10. The economy has recovered relatively fast from the 1997 crisis. This can be ascribed partly to the quick response of the government that undertook promptly economic restructuring and partly to the flexibility of wages. By the second half of 1999, GDP was growing at double-digit rates and unemployment was falling steadily. Employment increased by about 300 000 jobs by the end of 1999. Most new jobs were created in the service sector, which was also the one less hit by the crisis; employment in manufacturing increased by 100 000 jobs while the recovery of construction was slower. Wage increases were negotiated in June 1999. However, the strong recovery still leaves some scope for concern.

C. Current labour market challenges

11. Some observers have noted a certain complacency in the face of the economic recovery. This section shows that the labour market is still facing difficult challenges of a complex nature, which call for policy action.

1. A relatively low employment-population ratio

12. Korean employment-population ratios are low by international comparison. In 1998, the overall employment-population ratio was less than 60 per cent, that is 5 percentage points less than the OECD average (Table 1.3). The employment-population ratio of women is particularly low. This is due to the fact that many women withdrew from the labour market in the aftermath of the 1997 crisis.

13. These patterns differ considerably by age. Youth employment-population ratios are very low by international standards. There are no clear explanations for this: although youth enrolment rates have increased steadily over time, they are not higher than the OECD average (OECD, 1998). On the other hand, employment-population ratios of workers aged 55 to 64 are among the highest in the OECD average. This might reflect the fact that retirement pensions in Korea are modest, thereby leading Koreans to work until late in their lives.

2. *Groups at risk of unemployment*

14. Unemployment rates in 1999 are falling, however it is unlikely that they will return to the frictional 2 per cent rate recorded in the mid-nineties. Although unemployment rates on the order of 4 to 5 per cent, such as those recorded in early 2000, are low by OECD standards, singling out the groups more at risk of unemployment, and especially of long-term unemployment, is important for the purpose of economic policy.

15. *First*, it would seem that youth unemployment is structural in nature and that it will require policy attention. Unemployment rates of young Koreans aged 15 to 24 were much higher than unemployment throughout the eighties and the nineties, and they reached high levels in the aftermath of the crisis (Table 1.2). High rates of youth unemployment may reflect difficulties in the school-to-work transition.

16. *Second*, Korean unemployment has long been much higher among higher-educated workers than among their lower-educated counterparts, in contrast with the pattern prevailing in other OECD countries. However, since the crisis unemployment rates of the lower-educated have recorded a marked upward trend. Unemployment rates among workers with high-school educational attainment are relatively high, suggesting that high-school and vocational-training curricula might not adequately match labour market requirements.

17. *Third*, long-term unemployment -- defined as unemployment durations of over one year -- appears to be much less of an issue in Korea than in other OECD countries. This is probably explained by the low level of unemployment in the past, coupled with the absence, until recently, of any unemployment insurance system. Only 2 per cent of unemployed men and 1 per cent of unemployed women were unemployed for over one year in 1998, while in the same year 53 per cent of unemployed men and 62 per cent of unemployed women were unemployed for less than 3 months. Old-age workers are those most at risk of long-term unemployment in Korea. For the OECD as a whole, 32 per cent of unemployed men and 34 per cent of unemployed women were unemployed for longer than a year in 1998. In Japan, as well, the incidence of long-term unemployment is considerably higher than in Korea.

3. *Job precariousness and working hours*

18. A large proportion of Koreans are employed in “non-regular” jobs of short duration. In 1999, more than half of total employees had either a temporary or a daily contract, and the proportion of employees with a “regular” contract was therefore less than half (see Box 1.2 for definitions of “regular” and “non-regular” employment). A detailed analysis of employment by status suggests a degree of labour market duality by gender, age and education level, with younger and higher-educated men performing most regular jobs. The incidence of non-regular work is high among women, older workers and the lower-educated (Chart 1.3). The number of workers holding a permanent job was the lowest in Korea among OECD countries in 1998, followed by Turkey (Table 1.4). In 1999, 30 per cent of Korean workers had a regular job, less than half the share of regular employment in most other OECD countries. The share of non-regular jobs is the largest in the OECD, followed by Spain. The incidence of self-employment is among the highest for OECD countries together with Mexico and second only to Turkey where self-employment stands at 56 per cent of total employment. Unpaid family workers make up for about 10 per cent of self-employment in Korea and Mexico, 12 per cent in Greece and 25 per cent in Turkey, while this figure varies between 0 and 3 per cent in most other OECD countries.

19. Reflecting the high incidence of non-regular employment, average job tenure (*i.e.* the length of stay in the same enterprise) is low by international comparison. Average job tenure for men was about six

years in 1996 and 1997 and almost seven years in 1998, while average job tenure for women was less than four years in 1996 and 1997 and just over four years in 1998 -- in 1995, the unweighted average for OECD countries was 10.4 years for men and 8.4 years for women. It also appears that workers with a college degree enjoy longer job tenures than lower-educated ones (Table 1.5). However, tenure is higher for the lower-educated than for those with middle- or high-school education or junior college -- again signalling problems of school-to-work transition.

20. Koreans tend to work very long hours. The normal work week is 44 hours and includes six days. But a large proportion of employed individuals work over 54 hours per week -- the proportion came to nearly 50 per cent in 1997. By contrast, part-time work is not frequent. In particular, the proportion of women working less than 36 hours per week is much smaller than in many other OECD countries.

Box 1.2 Regular and non-regular types of employment

The Korean labour market is characterised by a sharp duality between “regular” and “non-regular” employment.

In the national statistics, regular workers are defined as employees that work for more than one year and are paid “regular” wages, meaning that they are paid the standard wage plus bonus and overtime pay. In the case of collective dismissals of regular workers, the employer has a legal obligation to notify government officials (see Chapter 2 for more details on lay-off procedures).

“Non-regular” employment refers to temporary and daily jobs. Temporary workers are employed for a determined length of time, usually longer than a month and shorter than a year. Daily workers are employed on a daily basis. In practice, most daily workers tend to be employed at a given establishment for longer than one day. In a few cases, mainly employment in the construction sector, daily workers are actually employed on some kind of spot market. Temporary workers and daily workers who are employed for longer than a month at the same establishment are, in principle, entitled to unemployment insurance (see Chapter 3). If they work over three months, they are entitled to early notification of dismissal (30 days). Entitlement to paid holidays depends on the length of employment, although all workers benefit from public holidays. Entitlement to sick leave may also be dependent on length of employment; for example, daily workers are usually not covered by sick leave arrangements.

As in other Asian labour markets, most Korean workers do not actually have a written work contract. The work contract is usually based on a non-written agreement between the employer and the worker. Some temporary workers, however, have a written work contract. The absence of a written contract of work may leave scope for abuse by employers who may report a worker as a daily or temporary worker, employed on a short-term basis, in order to reduce labour costs.

It has been argued that in the official statistics the distinction between the different categories of workers may be misleading. For example, sometimes it may be hard to draw a line between a temporary worker employed for longer than a year and a regular worker, or between a daily worker employed for longer than a month and a temporary worker. In addition, in the past separate statistics on temporary workers were not available, as those workers were classified in the statistics together with regular workers.

4. The labour market situation of women

21. As mentioned earlier, the employment-population ratio of Korean women is very low by OECD standards. In addition, women are more affected by job precariousness than is the case of men, and many of them work as unpaid family workers (Chart 1.3).

22. Moreover, a disproportionate number of women work in small firms (Table 1.6). In 1992, 71 per cent of employed women were working in firms employing less than ten workers, against 55 per cent in the case of men. This adds to the weak labour market position of women, as employment

protection is generally weaker in small firms than in large ones. It should be stressed that certain provisions of employment protection legislation were extended to all firms at the beginning of 1999 only.

23. Finally, despite progress, gender wage inequalities are large relative to other OECD countries.⁶ In 1990, average wages of women were about half those of men (Table 1.7). The gender wage differential was, however, slightly smaller in 1997, with average earnings of women being equal to 60 per cent of those of men. In 1997, the gender wage gap in Korea was the largest among the OECD countries for which data are available (OECD, 1999g, p. 83). Wage differentials by gender are much smaller for women with longer tenure and higher education levels: women with a university degree and over ten years of tenure earned on average 85 per cent of men in a similar situation in 1997. Finally, wages of lower-educated men increase with tenure much faster than is the case of wages of lower-educated women.

5. *Foreign labour in Korea*

24. The number of foreign workers in Korea is extremely low. However, it appears that foreign workers do not benefit from the same type of labour contracts and social security coverage as Korean workers. According to a survey of foreign labour in Korea, foreign workers often experience wage arrears (Kim, 1996).

25. Most foreign workers perform so-called “3-D” jobs (*i.e.*, jobs that are perceived as being dirty, difficult and dangerous), for which there is a shortage, notably at small and medium size enterprises. These jobs are concentrated in small firms in the labour-intensive manufacturing sector; particularly, in the beverage, clothing and fur, leather and shoe industries. According to a survey, Korean workers do not like to work in 3-D jobs because *a*) they dislike them (40 per cent); *b*) they are badly paid (20 per cent); *c*) working conditions are bad (12 per cent) or *d*) they have no information on these vacancies (12 per cent).

26. There were about 245 000 foreigners working in Korea in 1997. 33 per cent were “trainees”, 6½ per cent were skilled workers⁷ and 60 per cent were illegally established in the country.⁸ Their number fell to almost 160 000 by the end of 1998, as many foreign workers were expelled from the country, following the economic crisis and the steep rise in unemployment. In 1999, as the recovery got under way, the number of foreign workers increased again to about 186 000 in June 1999. However, in 1999 a special programme was started by the Korean government to subsidise firms that hire Korean nationals in the place of foreign workers⁹. This programme has had little success as only few companies applied for the subsidy given the small number of Korean workers that are willing to take up 3—D jobs (Park, 2000). It has been estimated that by September 1999 less than 17 per cent of the targeted replacements of foreign

6. On the basis of the Equal Opportunity Act adopted in 1989, employers are prevented from discriminating against women with respect to hiring procedures, career opportunities and pay. Furthermore, the Equal Opportunity Act was extended in January 1999 to include a Sexual Harassment Act, which seeks to establish a work environment favourable to women workers and respectful of gender differences. According to official estimates, almost 50 per cent of women in the population (including non-participants) were victims of sexual harassment in 1988 (source: Korean Institute of Criminology, in KWDI, 1998, p. 411). As these statistics relate to the period before Equality of Opportunity legislation was enforced, the current situation is bound to have improved considerably. However, more recent statistics are not available.

7. See OECD (1999h) for a more detailed account of trends in international migration.

8. The number of illegal immigrants is estimated by matching entries of foreign workers with exits of foreign workers in the registers of the Foreign Office—as anyone entering or leaving Korea is obliged to fill in some clearance forms.

9. The amount of the subsidy was set equal to 500 000 won per employee for a period of six months.

workers had taken place (Park, Y.B., 2000). The Korean government has currently doubled the amount of the subsidy. However, given the persistent shortage of labour in small and medium size enterprises, the number of foreign workers is unlikely to fall.

6. Multi-factor productivity and the growth prospects of the Korean economy

27. The prospects for increasing living standards depend crucially on the patterns of economic growth. Output growth, in turn, is mainly determined by *a*) the investment effort; *b*) the extent to which un-used labour supply can be mobilised in the economy; and *c*) multi-factor productivity growth. Interestingly, the fast growth experience recorded until 1997 was mainly based on the first factor, namely a spectacular investment effort. Thus, over the period 1990-96, Korea devoted 37 per cent of its yearly national income to real fixed capital accumulation. This is a very high figure by OECD standards -- it actually represents one of the highest investment efforts in the world. On the other hand, over the same period, multi-factor productivity practically stagnated, whereas it grew in nearly all other OECD countries. This is all the more surprising because multi-factor productivity is generally expected to grow faster in low per-capita income countries, as these countries acquire the new technologies already in use in highly developed countries -- the so-called catch-up theory. Few observers have pointed out that the low rates of multi-factor productivity growth are attributable to the fact that part of the investment effort may have gone into inefficient projects of doubtful productive value -- which is one factor behind the 1997 crisis. In addition, such high investment rates may not be sustainable over the medium-run, especially when they are financed by external borrowing as was the case in Korea.

28. It is therefore essential that future policy strategies focus on improvements in productivity, as well as a greater mobilisation of individuals who are presently on the margins of the labour market. The experience of other OECD countries suggests that such a strategy encompasses various training, labour and social policies, which are reviewed in the next chapter. Implementing these policies may have budgetary repercussions, but Korea seems to have some room for improving the efficiency of certain programmes (as will be seen below). In addition, taxes and other government revenues are relatively light in Korea (Chart 1.4) and there would therefore be some scope for widening the tax base, particularly as regards income taxes.

CHAPTER 2 INDUSTRIAL RELATIONS AND LABOUR LAW REFORM

A. Introduction

29. Industrial relations and labour law are important determinants of economic and labour market performance. Apart from influencing economic efficiency, industrial relations systems and labour regulations also pursue social goals, such as “fair” wages, “decent” working conditions and a healthy and safe working environment. The Korean industrial relations system and labour law, notwithstanding a legacy of authoritarian political regimes, have developed in a context of rapid real wage increases over the past several decades. Despite recent moves towards a closer adherence with international standards, Korean industrial relations and labour laws have particular characteristics that distinguish them from systems prevailing in other OECD countries.

30. This chapter reviews key features of the industrial relations system and ongoing labour law reform in Korea. It describes the main actors in labour relations -- trade unions, employer associations and the state -- and analyses trends in collective bargaining, wage determination and industrial conflicts. It highlights the evolution of industrial relations and labour law, from their previous emphasis on ensuring smooth industrialisation and economic development, to current policies to guarantee the autonomy of the bargaining system and to bring legislation in line with internationally-accepted standards. Finally, it discusses current challenges facing the Korean industrial relations system, as it seeks to achieve these objectives.

B. The actors in industrial relations

31. From a legal point of view, the basic pillars of the Korean industrial relations system are the 1948 Constitution which guaranteed workers the right to organise, bargain collectively and engage in industrial action, as well as four labour laws enacted in 1953 at the end of the Korean Civil War: the *Trade Union Act*, the *Labour Dispute Adjustment Act*, the *Labour Standards Act* and the *Labour Relations Commission Act*. Interestingly, these laws followed the liberal tradition of western industrialised economies, even though they were adopted when the economy was still largely agrarian. The latter two acts, while repeatedly amended, still exist today, while the former two were merged in 1997 into the *Trade Union and Labour Relations Adjustment Act*. The purpose of this Section is *a)* to briefly describe the historical background behind Korean industrial relations and *b)* to present the main actors in today’s system.

1. The historical legacy

32. In the three decades following the Korean War, industrial relations were primarily shaped by the government’s strategy for export-led industrialisation. After the advent of successive military governments in 1960, economic growth became the main priority under the slogan “develop first, share later”. The division of Korea and the threat emanating from the North was another crucial factor contributing to the

evolution of an authoritarian industrial relations environment. Certain workforce characteristics and values were conducive to worker acquiescence. There was an abundant supply of people migrating from agricultural areas to the new industrialising urban centres. These recent migrants were accustomed to working hard and long hours, and their wages were high compared with those of rural workers (Vogel and Lindauer, 1997; Woo, 1997).

33. Reflecting these political and socio-economic factors, labour legislation was amended with a view to ensuring labour peace and minimising the influence of trade unions which slowly but steadily increased their membership as a result of industrialisation.¹⁰ One of its features was the requirement for trade unions to affiliate to industry federations under a single, government-sponsored national centre, the Federation of Korean Trade Unions (FKTU). This quasi-monopolistic trade union structure, characterised by a close connection between union leaders, large employers and the government, was broadly maintained until the late 1980s. At the enterprise level, military rule tended to strengthen management prerogatives, while collective bargaining was little developed. The *chaebols* established hierarchical and paternalistic labour relations within the enterprise and succeeded in keeping their enterprise unions under tight control (Kwon and O'Donnell, 1999; Lee and Lee, 1999; Lee, 1999a; Lee, 1998; Park and Leggett, 1998; Wilkinson, 1994).¹¹

34. In addition, the intervention of “third parties” in collective bargaining and labour disputes was strictly forbidden. This was interpreted as prohibiting any interference by external parties other than the employees of a particular enterprise and, accordingly, led to the arrest of numerous trade unionists and their supporters. While the concept of the company and establishment level as the primary “locus of bargaining” also exists in other countries, for example Japan or the United States, this clause in Korean labour law carried the concept to an extreme. The fear of outsiders (such as agents of North Korea) supporting and “radicalising” trade union activities also led to the requirement that union membership be restricted to workers within a particular enterprise. In addition to these restrictions in the private sector, government employees and teachers did not enjoy the right to organise, and industrial disputes were forbidden in almost all public services and the defence industry.

35. As a counterpart to restrictions on freedom-of-association rights and collective bargaining, the government adopted or strengthened protective labour regulations to protect wages and working conditions which could not be determined through the operation of free collective bargaining. For example, occupational safety and health requirements and industrial accidents insurance were expanded, the scope of application of the *Labour Standards Act* was progressively widened to small enterprises, and in 1986 a *Minimum Wage Act* was adopted, applying to all firms with ten and more (since 1999, five and more) employees. In the early 1980s, a *Labour/Management Council Act* was also adopted, which aimed at creating a stable framework for labour/management consultation. Also, companies offered facilities and full pay for trade union officials as well as enlarged welfare rights for their workers: lifelong employment patterns, guaranteed bonus and other supplementary payments, company housing, etc.¹² In addition, a practice developed, without legal backing, for companies to compensate workers for their loss of salary during strike action, through back pay or other arrangements.

10. For example, in an effort to increase foreign investment, a special act on the restriction of labour disputes in 1970 guaranteed foreign companies a strike-free environment.

11. The *chaebols*, defined as multi-company business groups operating in a wide range of markets under common entrepreneurial and financial control, have been a driving force behind Korea's export-led growth and rapid industrialisation (see OECD, 1998, Chapter 3). The industrial relations system which they helped to design has been characterised as “corporatism within paternalistic enterprise structures” (Reddies, 1997, p. 499).

12. For example, the *Samsung* conglomerate offers, in exchange for a union-free environment, salaries and fringe benefits above market levels.

36. This situation was bound to change; as industrialisation progressed, workers became settled and the rural labour supply dried up during the 1980s. More fundamentally, starting in 1987, the political system moved towards democratic forms of government. Indeed, the Democratisation Declaration of June 1987 represented a turning point in Korean industrial relations, bringing to an end the so-called “management paradise” (Kim, S., 1999). At the same time, the issue arose as to whether a measure of “flexibility” should be introduced in labour regulations. Altogether, a slow process of labour law reform and democratic consensus building, gradually incorporating trade unions in national decision-making, was set in motion. In this respect, the February 1998 Tripartite Agreement has raised hopes for a stable and co-operative new industrial relations culture as called for by President Kim Dae Jung, although a number of, sometimes violent, industrial conflicts in the course of the economic crisis of 1997-99 have recalled the old confrontational spirits.

2. The trade union movement

37. As a result of the 1987 social movements, the Korean trade union landscape has undergone substantial change, although the influence of the authoritarian legacy described above still lingers on. The democratisation process brought with it an upsurge in trade union membership and activity. At the same time, the quasi-monopolistic trade union structure started to split up, as many enterprise unions broke away from the FKTU and labour activists set out to establish a rival trade union centre, despite the legal restrictions on multiple unionism. Federations of blue-collar and white-collar workers outside of the FKTU structure formed national organisations in the early 1990s, and finally merged in 1995 to establish the Korean Confederation of Trade Unions (KCTU), now the second national trade union centre. After several attempts to register with the authorities, the KCTU was certified by the government in late 1999, ending a precarious status bordering on illegality (see below for more details). Industrial affiliates could already register since 1997, after revised trade union legislation had allowed multiple trade unions at sectoral and national (but not at enterprise) levels.¹³

38. The FKTU has survived as the larger of the two centres, with 26 industrial federation affiliates as of end-1999, 3 500 organised enterprises and about a million members. The KCTU, in turn, has 19 industrial affiliates, is represented in 1 200 enterprises and has about half a million members, which means that its local unions are somewhat larger in size than those of its rival (KOILAF, 1999*d*). Over the past five years, this relation of strength has not substantially changed. Both unions are represented among blue-collar and white-collar workers and in industrial and service sectors, with the KCTU occupying strategic positions in automobile factories and shipyards. It remains to be seen how the two unions will adapt their strategies to the new possibility after 2001 to challenge their competitor as bargaining agent in individual establishments, and whether the relative strength of the two confederations will change as a result.

39. Both unions are in favour of the repeal of legal provisions which prohibit the payment of full-time union officials and do not allow dismissed workers to remain trade union members. They also oppose further reforms of labour regulations in the direction of a higher degree of “flexibility”, as well as industrial restructuring, including lay-offs, without full consultation of employee or trade union representatives.

13. To cite one example, now that rival federations at sectoral level are no longer prohibited, workers in the metal working sector are both represented by the KMWF (KCTU-affiliated, with 190 enterprise unions and over 190 000 members in 1998), and the FKMW (FKTU-affiliated, with around 500 enterprise unions and over 140 000 members).

3. *Employer associations*

40. Korean employers are organised in several associations. The oldest, founded in 1884, is the Korean Chamber of Commerce and Industry, which was given special status by an act of 1952, according to which all business owners gain automatic membership in the Chamber. The Chamber acts as a political/economic pressure group and, among other things, operates a number of vocational training centres.

41. The Federation of Korean Industry (FKI) is the representative of the large conglomerates (*chaebols*) and represents its members' interests, above all, in matters of economic policy. The key employer association in the area of labour, employment and industrial relations is the Korean Employers Federation (KEF), a nation-wide umbrella organisation which integrates numerous sectoral and regional employer and trade associations, as well as about 4 000 major enterprises. Its main function is to provide members with information and advice regarding labour legislation, labour/management relations and enterprise-level wage negotiations. It also participates in a number of tripartite organisations (such as the Labour Relations Commission and the Minimum Wage Council).

42. In contrast to the FKI, the KEF aims to represent the interests of both large and small businesses. However, the guidelines for collective bargaining which it submits annually to member companies, take little account of firm size (KOILAF, 1999*b*). Small businesses are also represented by a Korean Federation of Small and Medium-sized Business (KFSB), which represents the interests of over 2 million firms. Among other things, it advises and collaborates with the Korean government on the latter's important loan and subsidy programmes for SMEs and venture capital.

43. With the upsurge in trade union activity and production losses due to industrial conflict after 1987, business responded with numerous dismissals of union activists and a tougher line on back pay after strike action. During the 1990s, as a more balanced power relationship between labour and business gradually emerged, employers pursued new strategies to keep in check what they perceived as excessive features of trade union influence. Apart from limited experimentation with new forms of human resource management and more flexible remuneration patterns, employers have insisted, in particular, on a higher degree of quantitative labour market flexibility by enabling redundancy dismissals, as well as the need to curb their payments for full-time union representatives; both these demands were adopted through legislation in 1997, although the latter provision was not to come into effect before 2002.

44. Employers maintain that the current dismissal legislation is still too restrictive to allow sufficient structural adjustment. They are also resisting any attempt to weaken the prohibition of payment for union officers, arguing that without the assistance of the law, they are not sufficiently powerful to put an end to this practice through collective bargaining.

4. *Labour-management councils*

45. Korea is the only non-European OECD country that has legislated a works council statute, last revised in 1997 through the *Act on the Promotion of Worker Participation and Co-operation*. Works councils have received considerable attention in the literature as an institution of worker representation and labour-management communication which can provide effective "voice" to employees, even in non-unionised firms, and possibly also enhance workers' productivity (Rogers and Streeck, 1994; Freeman and Lazear, 1994).

46. Works councils ("labour-management councils") must be established in businesses or workplaces with 30 and more (initially 50 or more) employees; they are designed to maintain labour peace and to resolve actual or potential disputes at workplace level in a non-adversarial setting. The number of firms

setting up works councils grew rapidly after 1987, up to a point where currently over 90 per cent of firms which fall under the requirement have set up a council. Half of these firms are in the manufacturing sector. Almost all unionised firms have established works councils; however, as trade unions are only present in about 5 000 Korean workplaces, most councils operate in non-union settings.

47. The councils are composed of an equal number of employee and employer representatives; each side may have between three and ten members. In non-union settings, employees elect their representatives; when a union is present which represents over half of the workforce, it has the authority to nominate members on the council. Works council members are allowed time off work to prepare and participate in meetings; however, they do not have full-time status, even in the larger companies. Councils are required by the law to hold meetings every three months.

48. There is a long list of matters subject to consultation within the works council, from productivity concerns to recruitment, health and safety, and the introduction of new technologies. Certain items require the agreement of labour representatives, such as the establishment of a basic company training scheme, or the administration of company welfare facilities. The law distinguishes these matters from the collective bargaining function, but in unionised companies it is difficult to distinguish between works council and trade union activities. In addition, in certain non-unionised companies, the works council will engage in consultations (not much different from bargaining) over wage rates. The council also appoints a grievance-handling committee, again with equal representation of employer and employee members.¹⁴

5. The role of the state and tripartite arrangements

49. Government's role in industrial relations has changed with the onset of the democratisation process in 1987. However, between 1987 and 1997, the moves towards a comprehensive labour law reform were slow and social consensus-building was hampered by the continuing prohibition of trade union pluralism, *i.e.* the refusal to legalise new trade union organisations outside the FKTU monopoly. Important attempts to form tripartite institutions with a view to facilitate labour law reform were the Labour Laws Review Committee of 1992 and the Presidential Commission on Industrial Relations Reform established by President Kim Young-Sam in 1996. The latter body was the first to invite the participation of the KCTU, which was still not officially recognised. While there was a stalemate in the Presidential Commission on a number of the most important issues, it laid the groundwork for the partial labour law revisions of March 1997.

50. Labour law reform gathered momentum at the end of 1997 when a Tripartite Commission was created, under the auspices of President-elect Kim Dae-Jung, to help overcome the crisis. The Tripartite Commission, composed of representatives of labour, business, government and the public interest, rapidly found consensus on a number of key economic and labour issues; most of its agreements, made in a spirit of "fair burden sharing", were subsequently adopted by the National Assembly (see Box 2.1).

14. There is little analysis on the effectiveness of works councils in Korea *vis-à-vis* their purported aims of ensuring labour peace and preventing industrial conflict, or other items such as fostering productivity or job satisfaction. As works councils are mandated for all medium-sized and large firms, and there is a high compliance rate, there is little possibility to test for the impact of the presence, or lack of presence, of the institution. One study, using a data set compiled by the Korea Labour Institute, found significant associations between the existence of works councils judged as "effective" by both labour and management representatives, and measures of job satisfaction and labour productivity. However, there was no association with compensation, in contrast to the data showing significant wage premia in firms with trade union presence (Kleiner and Lee, 1997).

*Box 2.1 – Key Contents of the Tripartite Commission’s
“Social Compromise To Overcome The Economic Crisis”, February 6, 1998*

- 1) *Management transparency and corporate restructuring*
 - improvement of the corporate financial structure;
 - a more responsible and more transparent corporate governance;
 - promotion of business competitiveness
- 2) *Price Stability*
- 3) *Policies to promote employment stability and combat unemployment*
 - rapid expansion of financial resources for labour market programmes;
 - expansion and improvement of employment insurance;
 - livelihood support for the unemployed
 - expansion and improvement of the public employment service;
 - expansion of vocational training;
 - job creation through public works and business start-up subsidies;
 - consultation and re-hiring requirements in case of redundancy dismissals;
- 4) *Extension and consolidation of the social security system*
 - integration of social partners in social security steering committees
 - wage guarantee in bankruptcy cases
- 5) *Promotion of labour/management co-operation and respect for the autonomy of collective bargaining*
 - efforts to establish a more rational wage system, including profit-sharing
- 6) *Enhancing labour rights*
 - permission for public servants to form workplace associations;
 - permission for teachers to join trade unions
 - permission for trade unions to engage in political activities;
 - right of dismissed and unemployed workers to join trade unions;
- 7) *Enhancing labour market flexibility*
 - possibility for employers to dismiss workers in cases of managerial need;
 - permission for the establishment of temporary work agencies;
- 8) *Improvement of exports*
- 9) *Other issues, including*
 - the release of imprisoned trade union members,
 - regulatory reform,
 - corruption and money laundering.

51. In May 1999, the Tripartite Commission was given legal status by requiring that it be given the opportunity to review and comment on all policies of relevance for labour and employment.¹⁵ In this respect, the Commission now comes close to the status of tripartite or multi-partite Social and Economic Councils operating in many European countries, such as Belgium, France, Ireland or Portugal, which are all consulted during the drafting of social and labour legislation (see ETUI, 1990; Trebilcock, 1994). However, the succeeding Commissions have not experienced the consensus and stability of the first tripartite body, as trade unions and employer associations have repeatedly pursued an “empty chair” policy or threatened withdrawal if certain controversial items were put on the agenda. The current Third Commission, established in September 1999, plans to tackle issues such as the national pension and medical insurance system, the implementation of the President’s “productive welfare” concept, and enterprise bargaining under conditions of multiple unionism. However, it has not been able to function satisfactorily, due to repeated withdrawals, or restricted participation, of both employer and trade union representatives.

52. Another tripartite agency, composed of labour, business and public interest representatives, is the National Labour Relations Commission (NLRC), founded in 1953, which has recently been given increased autonomy, with its Chair elevated to Ministerial rank. The main functions of this Commission are adjudication of individual grievances, and mediation and arbitration of collective disputes. There were over 5 000 cases of adjudication in 1998, mostly concerned with unfair dismissals and unfair labour practices under the *Labour Standards Act* and the *Trade Union and Labour Relations Adjustment Act*.

53. Mediation committees consisting of three members representing labour, business and public interests are set up for each case of collective labour dispute. However, their decisions are not binding, and strikes are possible when their decision is rejected by one of the parties. By contrast, arbitration is mandatory for conflicts in “essential” public services, where previous mediation has not produced results. Arbitration committee members represent public interests, with no trade union or employer involvement.¹⁶

54. Apart from the above-mentioned agencies, more than a dozen tripartite or multi-partite advisory bodies used by the Labour Ministry, in the areas of employment policy, minimum wages and occupational health and safety, show the willingness of the Korean government to incorporate representatives of civil society in political decision-making.

C. Characteristics and outcomes of collective bargaining

55. In order to better understand the controversial debate on industrial relations and labour law reform, it is useful to examine recent trends in union density, collective bargaining and industrial disputes. The extent to which collective agreements have influenced wages is also addressed.

1. A concentration of unions in large firms and among regular workers

56. Chart 2.1 shows the evolution of trade union density (defined as the share of union members in wage and salary employment) and of the number of local unions after 1980. Notable is, first, the explosion of the number of local unions (*i.e.* mainly companies where the union is recognised as bargaining agent) between 1986 and 1989, from 2 600 to almost 8 000. However, in subsequent years, there has been a slow,

15. *Act on the Establishment and Operation of the Tripartite Commission*, passed on 24 May, 1999.

16. According to the NLRC, there were 105 cases of arbitration in 1998, of which 41 were solved with an arbitration award. The current NLRC leadership tends to avoid arbitration awards, encouraging instead voluntary agreements to avoid strikes in the public sector.

but continuous decline to a little above 5 000, still more than twice the number in the early 1980s. This compares to a figure of 190 000 firms in Korea with ten and more employees -- a measure of the overall trade union weakness. Similarly, trade union membership and density also grew substantially immediately after 1986 to peak at almost 19 per cent in 1989, but has been steadily declining thereafter to below 12 per cent, that is to levels not experienced since the 1970s.¹⁷

57. Within the OECD area, Korea thus has the second-lowest overall trade union density, after France and before the United States. Even in manufacturing, a backbone of union organisation in many industrialised countries, the Korean unionisation rate has fallen back to below 20 per cent. By contrast, the relatively high rate in transport and communication corresponds to the situation in other OECD member countries (OECD 1991, Chapter 4). More liberal labour legislation over the past few years seems not to have had a discernible impact, and it is difficult to predict whether the unionisation of teachers, the envisaged unionisation of other public servants and the planned lifting of the ban on multiple unions at company level will halt the decline.¹⁸

58. Despite the falling numbers of adherents, the trade unions' impact in the social and political arena is still considerable. This is, in particular, because union density in large enterprises is very high. As Table 2.1 shows, in 1995 four out of five trade union members were working in firms with over 300 employees. Another study on union membership from 1989 showed that, in 55 per cent of all firms of this size, trade unions were recognised as bargaining agents, and 60 per cent of the workers in these firms were unionised (Lee, 1998). Only about 5 per cent of union members come from companies with less than 100 persons. Where the union covers two thirds of the workforce, it has the possibility to negotiate a "union shop", whereby a new hire has to join the local union within a certain period of time; currently almost a third of all enterprise unions and half of all union members fall under such an arrangement.¹⁹ The high concentration of union membership and activity in the larger firms resembles industrial relations practices in Japan where, however, union density is twice as high as in Korea.

59. By contrast, Korean trade unions, in the absence of strong organisation at industry level, have found it hard to organise workers in small companies. According to the above-mentioned study, in 1989, union density was less than 2 per cent in firms with ten to 49 workers. In addition, few daily, temporary and part-time workers are unionised. For example, unionisation is almost nil in construction, an industry characterised by the use of day labourers. Finally, the share of women among union members is 20 per cent, compared to 30 per cent in the average OECD country.

60. Some local unions have made efforts to transform their organisational structure into industrial or sectoral unions, which are no longer legally prohibited. This has been successful in a few cases and indeed small industrial or occupational unions have emerged among scientific and technical workers, bus drivers

17. The slight upturn in 1998 is due to the contraction in employment, which apparently affected union members to a less extent than non-unionised workers. If the union density rate were calculated differently, by excluding public service employees (who cannot join unions) from the definition of "employee employment" in the denominator, it would be only a percentage point (*i.e.* not significantly) higher.

18. In many OECD countries, decline in trade union membership in the private sector since the late 1970s has been slowed or offset by union growth in the public sector, but this seems unlikely in Korea.

19. The large majority of union-shop arrangements are concluded by FKTU affiliates. To protect individual workers, the law permits an employer to retain an employee who has been expelled by the union. By contrast, there are no pre-entry *closed shops*, with the exception of the dock workers union which functions as a union "hiring hall".

and hospital workers.²⁰ However, as of today, less than 10 per cent of union members are organised outside enterprise unions.

2. A collective bargaining system mainly covering unionised enterprises

61. Collective bargaining is a process of decision-making between parties representing employer and employee interests which aims to establish “an agreed set of rules” to govern the terms of the employment relationship (Windmuller *et al.*, 1987). In Korea, as in the case of trade union membership, collective bargaining tends to concentrate in large enterprises and cover only a small share of all employees. This reflects the fact that, in Korea, collective bargaining takes place mainly at the level of the individual firm, where unions have bargaining power.

62. As is well known, there exist a wide variety of collective bargaining models in OECD countries. In the absence of legislation, the bargaining parties need to choose the appropriate *level*, or mix of levels, for their negotiations. In Korea, the enterprise was initially determined by law as the “locus of bargaining”, but remained so later through the voluntary decision of the involved parties. Only a small percentage of all collective bargains are not concluded at company, but at regional, sectoral or occupational level -- this is, for example, the case in the transportation industry (taxis and buses) and parts of the banking sector. True, there is some co-ordinating role of the national centres. Before the annual bargaining round, FKTU, KCTU and KEF usually publish guidelines for enterprise-level bargaining on wages and other employment conditions. In addition, the law allows enterprise unions to delegate bargaining responsibility to other actors, for example to their industrial federation, and particularly within the KCTU, demands are getting stronger to shift bargaining to the industrial level once and for all. However, such proposals (made for example in the metal industry) are meeting with strong resistance from employers who appreciate the flexibility implied in negotiations at company level. The Korean trade union movement does not currently have the required strength to enforce such a shift against the declared intentions of the business community, and the *chaebols* in particular. Also, there are simply no strong and resourceful employer associations at regional level, which could act as a counterpart of industrial unions. Altogether, among OECD countries, the Korean collective bargaining system is therefore in a common group with Canada, the United States, New Zealand and Japan, where bargaining tends to be conducted at company or establishment level with either no or limited co-ordination among bargaining agents, in contrast to sectoral or economy-wide bargaining characteristic in many other OECD countries (see OECD 1994, chapter 5).²¹

63. More than half of companies with over 300 workers, but less than 5 per cent of firms employing between ten and 100 workers are governed by a collective contract; furthermore, in firms with less than ten employees union membership and bargaining coverage are practically non-existent (Lee and Lee, 1999). Since there are no detailed surveys or administrative statistics on the extent of collective bargaining coverage, only an estimate can be given of the share of Korean workers covered by a collective contract. As a rule, it seems that the bargaining coverage rate in Korea is not substantially higher than the trade union density rate, which would correspond to the situation in Japan and the United States. Nevertheless, a certain number of factors are at work to increase somewhat the proportion of workers under collective agreements over those adhering to trade unions.

20. The KCTU, for example, has stated in its charter the resolve to “...construct an industrial trade union system and unify all of the trade union movement”.

21. Japan is usually considered to have the highest degree of co-ordination in firm-level bargaining among the countries listed. While there is evidence to the effect that bargaining levels are shifting downwards (for example concerning flexible work practices and working time arrangements), it seems that in a majority of OECD countries the sectoral level has remained the principal arena for wage determination (see Katz, 1993; OECD, 1994; Clarke, Bamber and Lansbury, 1998).

64. The law requires employers in companies where over half of the workforce is unionised to extend the contract to the total workforce in the firm. Data supplied by the Ministry of Labour imply that in 1998 about 350 000 workers were thus additionally covered in the 4 000 companies where this was the case. Based upon experience in other industrialised countries, it can be assumed that employers do not usually pay different wage rates to unionised and non-unionised workers even in firms where, say, the local union represents only a third or a quarter of the workforce. This, and possible extensions by the Labour Ministry of the few regional or sectoral collective agreements to employers and employees not affiliated with the bargaining parties, may increase the number of covered workers by another small percentage. On the other hand, it can be assumed that a certain number of union members belong to local unions which have not (yet) gained bargaining status and will therefore not be covered by a collective contract. In any event, considering that about 1½ million Korean workers are organised in trade unions, no more than 2 million or 16 per cent of dependent employment can be estimated to fall under collective agreements, the lowest share within the OECD area, below even the United States and Japan (OECD, 1997a, Chapter 3). A certain additional proportion will be covered through the “quasi-bargaining” mechanism in labour-management councils.

3. *Industrial conflicts*

65. Labour disputes and dispute resolution are extensively regulated in Korea. In case of an impasse in collective bargaining, the local trade union and/or the employer need to file a request for mediation with the local Labour Relations Commission, after which a cooling-off period of ten days (15 days in public services) applies. Under no circumstances can collective action start before a decision has been made by a majority of the workforce concerned. Wildcat strikes and occupation of production facilities, as well as the replacement of strikers with workers outside the business, are prohibited. The lockout is recognised as a defensive weapon.

66. Chart 2.2 shows strike days per 1 000 workers in Korea and four other OECD countries since the early 1980s. It is evident, first, that strike activity in Korea, after stagnating in the early 1980s, grew explosively in 1987, after the Declaration of Democratisation. The lost workday ratio grew from eight per 1 000 workers in 1986 to almost 800 in 1987, and the number of persons involved grew from less than 50 000 to almost 1.3 million. In the two months following the Declaration in June 1987, there were as many strikes as in the preceding two decades.²²

67. After remaining at high levels up to 1989, the number of strikes and of lost workdays progressively declined, almost to pre-1987 levels, before turning up slightly during the recent economic crisis. As the chart also shows, however, even in 1987 to 1989, Korean strike rates did not reach the levels experienced in the 1980s by OECD countries such as Italy or the United Kingdom. With about 80 lost workdays per 1 000 workers on average during the period from 1993 to 1998, Korea now occupies a middle position among OECD countries, on a level with Ireland, Norway, Sweden and Australia (Davies, 1999; ILO, 1999).

68. As illustrated in Table 2.2, the share of wage demands among the causes for industrial conflict has gradually declined since the late 1980s. The major category since 1995 are contract-related issues which include, *inter alia*, the reduction of working hours, payment of union officials, union shop issues,

22. As Wilkinson (1994) notes, citing Korean observers, in 1987 to 1989 the mood of the labour movement was one of “strike first, negotiate later”; many of the strikes took place before the expiration of existing collective agreements and were illegal in one way or another. An analysis of the reasons for worker unrest in 1987, under the heading of “why were workers so angry”, can be found in Vogel and Lindauer (1997).

and back pay after strikes. Notable is also the increase in strikes for issues relating to firm closures and deferred wage payment after the onset of the recent economic crisis.

69. Data are also available on industrial conflict by industry and firm size. As a rule, four out of five disputes occur in only two industries, *i.e.* manufacturing and transport and communication. Also, on annual average at least as many strikes occur in firms with 1 000 or more employees (where only 10 per cent of Korean wage and salary workers are employed), than in firms with up to 100 workers (where over 70 per cent are employed). These statistics throw additional light on the trend towards concentration of union activity.

4. A high degree of wage flexibility

70. As discussed in Chapter 1, real wages show a considerable degree of responsiveness to the labour market situation. Between 1985 and 1997, a period characterised by tight labour markets, the average real wage doubled -- an increase without parallel in OECD countries. On the other hand, real wages were cut by about 10 per cent in response to the crisis. This included the wages of regular workers falling under collective agreements. Declines in real wages of such a magnitude are very unusual in other OECD countries. They suggest that the collective bargaining system in Korea has contributed to a high measure of wage flexibility.

71. Collective bargaining has also contributed to the evolution of remuneration patterns and wage differentials:

- As noted by certain analysts, the Korean system of wage payments has become very complex (Kim, 1995).²³ Chart 2.3 shows the evolution of the three fundamental components of total wages -- regular fixed pay, overtime pay and bonuses -- over time. The share of bonus pay has increased from 12 per cent in 1980 to almost a quarter of total remuneration in 1996, before falling back to below a fifth in the crisis year 1998. Some Korean companies, particularly within the *chaebol* structure, pay much more in bonuses than is apparent from the above average; fairly typical among top *chaebol* companies seems to be a total bonus corresponding to six or seven monthly salaries, paid out in three or four instalments throughout the year (Lee and Rhee, 1996). The trend-rise in bonuses and special allowances is partly explained by the fact that, in the early and mid 1990s, the Korean government, concerned about business competitiveness, proposed wage targets to the collective bargaining parties. While the KEF and FKTU participated for a while in the government-led incomes policy, many companies and enterprise unions ignored the targets or circumvented them by restricting their application to the basic salary (thus claiming to fulfil government targets), but not observing them for the bonus or other special allowances. The Korean government continuously encourages the social partners to simplify the wage structure by consolidating the multiple allowances, and increasing the proportion of basic wages in total remuneration (KOILAF, 1999b). However, the increasing share of the bonus, which is at least partially related to cyclical conditions, has also made the wage system more flexible. For example, in 1998 regular pay still showed a small nominal increase, while in response to the deteriorating financial position of companies, bonus pay decreased by almost 20 per cent. The situation was reversed in the 1999 upswing, when regular pay increased by 6 per cent, and bonus pay by over a quarter.
- There is strong evidence of changing relative wages accompanying the high wage growth over the past two decades. Full employment patterns, the widespread availability of education and trade unions'

23. For example, it has become difficult to determine on which wage components to calculate income tax and social security contributions (Lee, 1999a).

bargaining power have contributed to a reduction in wage differentials, which nevertheless remain significant (Chart 2.4). Although age and seniority within a firm continue to be major factors in determining wages and promotion patterns, the relative pay of workers aged 40 and over has declined substantially compared with younger age groups.²⁴ Craftsmen and production workers have considerably reduced the wage gap to white collar employees; similarly, the premium for education has narrowed as a result of the rising numbers of college and university graduates. The female wage gap in Korea has also decreased over time, which may reflect greater demand for female workers in the expanding service sector, as well as the passage of the *Equal Employment Act* in 1988; however, as Chapter 1 has already pointed out, it remains the highest among OECD countries, where the corresponding data are available. By contrast, the Chart illustrates the widening disparities in earnings between workers employed at small (ten to 29 employees) and large (over 500 employees) enterprises, which may reflect an increasing recourse of the larger employers' to paying efficiency wages, but also the impact of unions which, as shown earlier, are concentrated in large firms. This wage premium increased particularly between 1986 and 1991, up from a level of only 10 per cent, but seems to have stagnated at around 40 per cent since then. Latest statistics show that workers in large firms (with over 500 employees) again received the highest wage increases during the 1999 upswing²⁵.

72. As illustrated in Table 2.3, low wages seem to have been little affected by the minimum wage system which was first introduced for manufacturing in 1988 and later extended to firms in all industries employing ten or more (since 1999 five or more) workers. The minimum wage level is set by the Labour Minister after a recommendation by the tripartite Minimum Wage Council. The current level of 1 600 won per hour corresponds to less than a quarter of average wages in the manufacturing industry (including overtime payments and special allowances), a slight decrease from the beginning of the decade. This ratio is among the lowest (with Mexico and the Czech Republic) of OECD countries where data are available.²⁶ The number of Korean workers covered by the minimum wage has fallen to half a per cent of all wage and salary earners, which corresponds to less than 1 per cent of those working in firms with 5 and more employees. No data exist on workers' pay levels in those Korean firms that employ less than 5 employees, but it can be assumed that the share of workers paid at minimum wage level would increase significantly if these firms were included.

D. Recent labour law reforms

73. Since the mid-1990s, first under President Kim Young Sam and since 1998 under President Kim Dae Jung, the Korean authorities have adopted several reforms in the area of industrial relations and labour law. The purpose of these reforms has been to improve freedom-of-association rights and to enhance numerical labour market flexibility. As was outlined above, in the past a high degree of employment security had acted as a corollary to restrictions in trade union rights. With the labour law revisions of December 1996 and March 1997, as well as the 1998 agreement of the Tripartite Commission in the wake of the economic crisis, substantial changes were set in motion in both these areas. Importantly, after initial failure, a delicate balance between flexibility measures and improvements in trade union rights was struck in the Tripartite Agreement which was able to enlist the support of business and (albeit less enthusiastically) labour organisations.

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24. An international comparison in OECD (1998a) shows, however, that the age-earnings profile of Korean blue-collar workers is still steeper (and the age premium higher) than in many other OECD countries, including Japan where average earnings peak much later.
25. All Korean wage data need to be analysed under the caveat that they usually do not cover firms with less than ten employees.
26. OECD Minimum Wage database, data referring to 1997.

1. *Employment status and protection*

74. The *Labour Standards Act* of 1953 (LSA) is the main piece of legislation which regulates working conditions and employment contracts. As a rule, it applies to companies with five or more staff, *i.e.* to about 70 per cent of total dependent employment. A number of its provisions do not apply to daily and other short-term workers; for example, notice periods do not apply to probationary periods, most daily workers and employees under short-term contracts, while legal severance pay provisions do not apply to employment relationships of less than one year duration. By contrast, other provisions defined in a Presidential ordinance (on equal treatment, wage payment, rest periods and holidays, for example) apply to all workers, including those in firms with less than five staff (for more detail, see Hyun, 1999). While most of these regulations remained broadly stable over the 1990s, major changes occurred in the area of dismissal protection for regular workers. In addition, labour market flexibility was enhanced through the legalisation of temporary work (so-called “dispatch”) agencies.

Employment protection for regular workers

75. Under the *Labour Standards Act*, individual and collective dismissals of regular employees (usually those with an open-ended contract, currently less than half of dependent employment) are allowed for “just cause”. Dismissal for non-performance or lack of competence has therefore always been possible in Korean law, but was rare in practice, since the Labour Relations Commission (the initial appeals board in dismissal cases) and the courts have in the past applied high standards *vis-à-vis* the “just cause” provision.

76. The Act entitles employees to a 30-day notice period or wages in lieu, and to generous severance pay (retirement allowance) equal to at least 30 days per year of service. This severance payment must be made regardless of the circumstances of termination, even in the case of dismissal with just cause. Many firms exceed this requirement; they may pay, for example, 40 or more months wages to an employee with 30 years tenure. In the past, severance pay was the functional equivalent of pension income and even after the public pension system was introduced in 1988, it continues to play an important role in assuring retirement income²⁷.

77. The 1998 agreement in the Tripartite Commission led to the rapid introduction of a major revision to the LSA by introducing the concept of redundancy dismissal and employment adjustment for “urgent managerial needs”, which are further defined by a reference to “transfers, mergers and acquisitions” (art. 31).²⁸

78. The 1998 Act also specifies that, prior to layoffs, employers must make every effort to avoid dismissal; apply fair standards in selecting employees for dismissal; and consult with trade unions or other worker representatives on efforts to avoid dismissal and on fair and reasonable selection criteria (LSA, art. 31).

79. Worker representatives have to be informed 60 days prior to planned dismissals for managerial reasons. When recruiting new personnel at a later stage, an employer shall make efforts to rehire dismissed workers within a period of two years after the date of dismissal. Collective dismissals involving larger numbers of workers give rise to additional requirements; in these cases, the company also needs to notify

27. A revision of the LSA in 1997 allowed the receipt of interim severance payments during the course of employment.

28. While the provision was introduced into the law in March 1997, its implementation had initially been suspended for two years.

the Ministry of Labour 30 days in advance, providing the rationale for lay-offs and proof of sufficient consultation. Such notification is required if lay-offs exceed more than ten employees in a workplace with less than 99 workers; more than 10 per cent of employees in a workplace with 100 to 999 employees; and more than 100 employees in workplaces with over 1 000 workers.

80. Under a separate act, a Wage Claims Guarantee Fund was established in 1998 to protect workers dismissed from bankrupt enterprises from loss of income and severance pay. Maximum payments by the fund are equivalent to the sum of wages for the last three months and severance pay for the last three years before bankruptcy. The Fund is financed mainly through an employers' contribution, set at a level of 0.2 per cent or less of the wage bill.²⁹

81. While the new layoff provisions are clearly a step in the direction of increasing the freedom for firms to shed surplus employees, the current level of employment protection regulation for regular workers, as outlined above, is still higher than the OECD average. The newly added preconditions for layoffs, as well as the remaining difficulties in reaching consensual decisions and procedures between management and enterprise unions, continue to restrict firms' room to manoeuvre when adjusting to structural changes.³⁰

82. A detailed international comparison of employment protection provisions for regular employment draws the following picture. First, while the one-month notice period, even for workers with high tenure, is low by international standards, the severance pay regulation for workers in medium-sized and large companies would seem to be relatively generous, although its origin as a replacement of both pension and unemployment insurance benefits has to be kept in mind. As the unemployment insurance system will become more firmly established and the public pension will become more mature, there seems to be room for easing the legal severance pay requirements for regular workers.

83. Next, even though economic reasons may now constitute a "just cause" for lay-offs, the newly legislated preconditions for such dismissals (advance notification to trade union, verifiable efforts to avoid dismissal, etc.) still make Korea resemble other high-protection OECD countries such as Japan, Portugal, France or Germany. Finally, the new provisions on notification of collective dismissals to the head of the local labour office correspond to regulations prevailing in the European Union. The language in the Korean Act nevertheless seems somewhat less restrictive than in many European countries, which provide for the negotiation of "social plans" in case of collective dismissals. After scoring the country on these and other features of regulation, a recent OECD study ranked Korea 26th out of a sample of 27 OECD countries in terms of the strictness of protection of regular (permanent) employment contracts (see OECD 1999a).

Employment protection for non-regular workers

84. Employment protection for workers without a permanent employment contract is much weaker than for their regular counterparts. The result is a share of fixed-term and daily workers in dependent employment which, at over 50 per cent, is the highest in the OECD area.

85. In the case of workers with fixed-term contracts, the OECD ranked Korea on a middle position among OECD countries (OECD 1999a). The LSA permits fixed-term contracts of up to one year duration

29. As of December 1999, over 17 000 workers at 460 establishments had been awarded payments from the fund. These were mostly prime-age males from the manufacturing and construction industries (data specially submitted by Ministry of Labour.)

30. For example, even at the peak of unemployment in the spring of 1999, only a minority of total unemployment was due to redundancy dismissals (see Chapter 1).

without specifying an objective reason (which is necessary, for example, in many European countries). Longer contract durations are only allowed for the “completion of a certain project” and, as in many other OECD countries, several successive renewals run the risk of a court declaring the employment contract null and void. However, jurisprudence seems not too rigid on this issue and employers seem to face no major difficulty in circumventing the existing restrictions.

86. Employment flexibility has been further enhanced by the decision to allow temporary work agencies under the *Dispatched Workers Act* as from July 1998. Dispatching agencies are allowed to hire out workers to user firms for up to two years in 26 occupations that require special expertise and experience. In addition, an employee may be hired out in *all* industries and occupations in order to fill vacancies due to temporary absences of other employees, with the exception of construction, seafaring and hazardous occupations.

87. Certain restrictions to the employment of temporary workers apply to user enterprises. For example, before filling vacancies due to temporary absence of regular employees with temporary workers, the employer has to engage in sincere consultations with labour representatives. Also, without trade union consent temporary workers cannot be used on a post for a period of two years after dismissal of the previous post-holder.

88. At the end of 1998, the Ministry of Labour reported the number of licensed agencies at about 800 and of hired-out personnel at 42 000. Other estimates give a much higher figure of temporary workers, which include those by illegally run agencies operating even before the adoption of the 1998 legislation (Hyun and Balfour, 1998).

89. As Chapter 1 has shown, the share of fixed-term, temporary and daily workers increased further during the recent economic crisis. It seems that during the current upswing employers, unsure about the prolonged character of the recovery, are making full use of opportunities given by the law for avoiding permanent employment contracts. This strategic choice may also be due to employers trying to avoid the high rates of severance pay for permanent employees in case of future restructurings and retrenchments³¹.

2. Labour relations and trade union rights

90. Greater flexibility in allowing layoffs and the operation of temporary work agencies was accompanied by increased rights for labour unions. Indeed, this *quid-pro-quo* was one of the main elements of the February 1998 compromise agreement in the Tripartite Commission and the preceding Tripartite Statement on fair burden-sharing. Much of the labour unrest in the past two years seems to be due to sentiments among many workers and trade union officials that the measures decided on both accounts were not equitably implemented.

91. Nevertheless, there is no doubt that after the controversial and unsuccessful labour law reform bill passed in the National Assembly in late December 1996, the two subsequent reform packages of March 1997 and February 1998 have moved Korean industrial relations and labour regulation away from its authoritarian legacy and closer to internationally-accepted standards.³² For example, the principle of trade union pluralism has been recognised, teachers have been given the right to organise, and the previous ban

31. Notably, up to the crisis, the use of precarious contracts seems to have been much less pronounced in larger firms with established union representation.

32. Under the leadership of President Kim Dae Jung, a certain number of reform issues could be tackled in the Tripartite Commission which had led to stalemate in the previous Commission on Industrial Relations Reform set up under President Kim Young Sam.

on political activities of trade unions has been entirely lifted. The most important remaining problem areas will be briefly outlined below.

Multiple trade union representation

92. Up to 1997, trade union legislation specified that only one trade union was permitted at company, industry and national levels, and that rival unions which tried to organise the same potential membership as existing ones were prohibited. As newly formed trade unions were required to register with the authorities, these withheld recognition in multiple cases. Trade union centres and federations, particularly the Korean Confederation of Trade Unions (KCTU) and its sectoral affiliates, which were formed outside the framework of the long-established Federation of Korean Trade Unions (FKTU), were therefore legally and practically disadvantaged; in addition, it proved practically impossible for new trade unions emerging at local level to challenge the position of established unions as bargaining units in a particular enterprise.³³

93. Basing its judgement on Conventions 87 on Freedom of Association and 98 on the Right to Organise and Bargain Collectively (which have not been ratified by Korea, an ILO member since 1991), the International Labour Organisation has held that the prohibition of multiple trade union representation in Korea does not conform to international norms and practices.³⁴

94. The revised 1997 *Trade Union and Labour Relations Adjustment Act* (TUULRA) allowed multiple trade unions at industrial and national levels, which ultimately paved the way for the legal recognition of the KCTU (see Box 2.2). By contrast, on the *enterprise level*, multiple unions will only be allowed from January 2002 onwards. This delay seems to be due to the Korean government's concern about possible inter-union rivalry and recognition disputes between FKTU- and KCTU-affiliated trade unions. The Ministry of Labour has been given the legislative mandate to "introduce methods ... to establish a single bargaining channel by December 31st, 2001" (TULRAA, Addendum, art. 5). This mandate was meant to prevent a situation where an employer would be forced to bargain separately with several unions in his enterprise. To comply with the legislation and prepare for the co-existence of multiple unions at company level, the Korean authorities can choose between several models of union recognition for bargaining purposes which exist in different OECD countries. For example, in the United States and Canada one union is recognised as the exclusive bargaining agent, usually after winning a majority in representation elections. Another model is characterised by different trade unions forming a joint committee to bargain with an employer or employer association. This system prevails in a number of European countries where the status of "most representative trade unions" may be based on the number of adherents within an enterprise, or on participation in national consultative bodies.³⁵

95. In late 1999, after meetings with representatives of public interest, the Tripartite Commission has presented a proposal to the government concerning the future bargaining set-up under conditions of multiple unionism. This proposal mixes the two models outlined above. As a general rule, the trade unions should themselves autonomously define the "single bargaining channel". They can choose the committee

33. The KCTU could only establish itself as bargaining agent in previously non-unionised firms, or when previous FKTU affiliates decided to switch allegiance.

34. Other OECD countries that have not ratified these key conventions are New Zealand and the United States (both Conventions), and Canada, Mexico and Switzerland (C. 98). Korea has, by contrast, ratified three other conventions defined as fundamental by the International Labour Organisation: Cs. 100 and 111 on the prohibition of discrimination; and C. 138 on child labour. It has ratified nine of 182 Conventions overall.

35. Biagi (1998) gives a detailed account of the various models of union recognition for bargaining purposes prevalent in OECD economies.

model, where representatives of several unions bargain jointly with the employer. By contrast, if they cannot come up with unified representation, the union which represents the absolute majority of total union members within an enterprise will act as bargaining agent. If such a union does not exist (a situation that will probably be rare, considering the KCTU/FKTU duality), the composition of the bargaining unit will be decided by Presidential Decree. The Korean government has submitted a draft bill containing the Commission's proposals to the National Assembly.³⁶

Box 2.2. The process of legal recognition of the Korean Confederation of Trade Unions (KCTU)

After the democratisation movement of 1987, labour activists tried to establish a national trade union centre outside of the structure dominated by the Federation of Korean Trade Unions (FKTU). In 1995, several national confederations of blue-collar and white-collar workers merged to establish the Korean Confederation of Trade Unions (KCTU). Although this new organisation accounted for one third of total union membership in Korea, it was not legally recognised by the Korean authorities due to the prohibition of multiple unionism under the Trade Union Act.

The revised Trade Union legislation of March 1997 permitted multiple unions at national and sectoral levels. However, even after this reform applications for registration by the KCTU and several of its affiliated sectoral unions were rejected on a number of occasions. The main reasons given for the non-recognition of the KCTU were that an illegal body -- the teachers union (Chunkyojo) -- was affiliated to the organisation and that certain dismissed workers or other persons not currently employed were among its elected officers. Despite its ambiguous legal status, the KCTU has been actively involved in collective bargaining and has been invited as an equal partner to the Tripartite Commission. However, its participation in other advisory bodies to the Korean government has been limited, and it has not received the kind of government support for vocational training and other activities that the FKTU has enjoyed. In addition, KCTU members and officials have frequently been charged with illegal strike action and violent conduct, and been the subject of arrest and imprisonment.

After legislation permitting the establishment of teachers unions took effect in July 1999, the inclusion of Chunkyojo among KCTU affiliates was no longer an impediment to the union's legal recognition. However, a new application of the trade union was again rejected on the ground that one of its Vice-Presidents was a dismissed worker. In November 1999, the Korean government finally recognised the legal status of the Korean Confederation of Trade Unions, upon its fifth application for registration with the Ministry of Labour.

This decision has been generally welcomed as an important gesture by the Korean authorities with a view to reducing worker disenchantment and labour strife; it should also pave the way for an enhanced role of the KCTU in national dialogue, and for more equitable treatment of the two trade union centres in the years to come. However, it seems appropriate to recall that, as long as the law prohibiting union membership of dismissed or unemployed workers has not been modified, cases of non-recognition of trade unions who admit such workers among their ranks or leadership, may arise again (see further below).

Third-party intervention

96. The 1997 TULRAA removed the previous ban on third-party intervention and replaced it with provisions which specify those categories of persons who, while not being members of the local bargaining unit, may assist trade unions and employer associations in collective bargaining or cases of industrial conflict. The categories of authorised persons listed in the law include members from sectoral or national-level trade unions and employer associations. However, the names of other persons who assist the bargaining parties have to be notified in advance to government authorities. Persons other than those notified are still prohibited from intervening. This requirement has no parallel in other OECD countries.

36. It seems safe to say that once multiple unionism at enterprise level will be institutionalised in 2002 along this or a similar model, freedom-of-association principles in the private sector will be widely respected in Korean labour law and practice (see further below for remaining problems in public services).

97. The Korean authorities maintain that the notification clause is meant to guarantee the autonomous resolution of labour disputes between management and labour and to prevent any intervention or manipulation by outsiders unwanted by the parties to the particular conflict. They also note that advance notification does not imply a necessity for “approval” or “permission”, and that employer and employee associations can choose whomever they want to assist their activities. It appears, however, that the notification requirement is not a pure formality since non-notified persons who intervene in collective bargaining or labour disputes are liable to a maximum penalty of three years imprisonment or a fine of up to 30 million won (TULRAA, art. 89). The ILO's Freedom-of-Association Committee continues to be concerned that the provision entails serious risks of abuse and that circumstances could arise where the “notification” would be interpreted as an “authorisation” requirement. The Korean government, for its part, has complained that the number of third-party advisers notified by trade unions is sometimes so large as to contradict common sense (for example, in a 1998 case over 84 000 advisers were notified by one local union with a membership of only 330; cf. ILO, 1998).

The right to organise and bargain collectively for public servants and teachers

98. Following on from the Trade Union Act, the 1997 TULRAA states that “workers are free to establish a trade union or to join it, except for the case of public servants or teachers who are subject to other enactments” (art. 5). Accordingly, the Public Services Act has prohibited public officials from joining trade union organisations. This provision refers to all levels and categories of government personnel, with the exception of manual workers employed mainly in telecommunications and the national railroads.

99. Following agreement in the Tripartite Commission in February 1998, an *Act Concerning the Establishment and Operation of Workplace Associations for Public Officials* was adopted by the National Assembly which allowed the establishment of workplace associations in the public service from January 1999. As of late 1999, 60 workplace associations had been established in central and local government.

100. The main purpose of these associations consists of consultation over working conditions and grievance-handling. The Act restricts the right of association to the lower four out of nine grades of public officials, since grades 5 and above are considered to be comparable to managers in the private sector. Police, firemen, security guards, chauffeurs, and other categories of officials involved in, *inter alia*, personnel administration, budgeting and accounting are also not permitted to join the associations. In total, over one third of public service personnel is thus ineligible.

101. The agreement in the Tripartite Commission also envisaged that, after some stock-taking of the experience with workplace associations, trade unions endowed with bargaining rights would be allowed to form at national, provincial and local level. The legal status of future collective agreements within the public service remains to be determined.

102. *Teachers* have already been granted trade union status. Before 1999 only teachers associations were allowed which were consulted over working conditions, but did not have the right to conclude collective agreements. Following agreement in the Tripartite Commission, a law on the *Establishment and Operation of Trade Unions for Teachers* took effect from July 1999, which granted teachers unions the right to bargain collectively over wages and working conditions³⁷. However, in the case of public school

37. Accordingly, the Korean Teachers and Educational Workers Union (Chunkyojo), affiliated to the KCTU, which had been considered an illegal organisation, can now operate without restrictions, while an FKTU-affiliated teachers union, the Korean Union of Teaching and Education Workers, has also been established.

teachers, the Korean National Assembly keeps the final say in setting pay rates, and any strikes are prohibited.

103. The ILO's Freedom-of-Association Committee has taken issue with the prohibition of managerial/administrative staff to join employee associations, since it has previously judged, based on C. 87 and C. 151, that only "persons exercising senior managerial or policy-making responsibilities" could arguably be excluded from trade union membership. C. 87 on Freedom of Association guarantees the basic right to form and join organisations of their own choice to all workers "without distinction whatsoever", including public servants. C. 151 concerning the Right to Organise in the Public Service confirms this requirement and requests governments to "promote the full development and utilisation of machinery for negotiation of terms and conditions of employment between the public authorities concerned and public employee organisations..."

104. Most other OECD countries have recognised the right of public servants and teachers to organise in trade unions or other types of employee associations; however, important restrictions remain in many cases with respect to certain personnel categories, the nature and scope of bargaining (particularly on pay issues) and the right to reach collective agreements (Treu, 1987). The military, police and judges, in some cases prison guards, are typically excluded from the right to organise in most countries. Agreements reached through collective bargaining in the public service often acquire legal status only after approval by government or parliament. Consequently, only half of OECD countries have ratified C. 151, and even some of these have been judged by ILO Committees to be in contravention of the relevant ILO instruments.

105. While many OECD countries do not conform fully to the requirements of these conventions, Korea remains unique in that it *a)* does not recognise the right of public officials to join trade unions; and *b)* even restricts membership in consultative workplace associations to support staff alone. Much will depend on the speed with which trade unions will be allowed to form in the public sector, in the spirit of the 1998 Tripartite Agreement (there are currently no concrete plans or timetable on this issue). But the restrictions of trade union rights in the public service could imply that, even after the removal of the ban on multiple trade unions at enterprise level in 2002, Korea will be judged as remaining in contravention of basic freedom-of-association principles.³⁸

The right to strike and compulsory arbitration in the public sector

106. The 1997 TULRAA and special public service legislation prohibit strikes by workers in central and local government and those engaged in the production of military goods. The act also restricts the right to strike in the more broadly defined public sector by providing for special mediation and arbitration proceedings for two kinds of public service enterprises;

- *Ordinary "public service enterprises"* are defined as including regular public transportation services; gas, electricity and water; oil refineries and oil supply; hospitals and other medical services; banks and

38. To take an example among OECD countries, in Germany even higher-level officials in public service can join the *Beamtenbund* (civil servants federation), a type of trade union not endowed with the right to strike, but which nevertheless negotiates with Interior Ministries at federal and Land level about wages and other employment conditions. Since officially wage rates remain determined by parliament, this type of negotiation has been termed "quasi-bargaining" where, in effect, wage increases have moved along with rates bargained in the private sector, or for public sector employees not endowed with *Beamten* status.

the Mint; and broadcasting and communication. In cases of pending industrial conflict, ordinary strike regulation applies (mediation by the Labour Relations Commission and cooling-off period).

- “*Essential public services*” are those where strikes “may endanger the daily life of the general public or undermine the national economy considerably”. In these enterprises, the Labour Relations Commission, after recommendation of a special mediation panel representing public interests, can invoke *compulsory* arbitration after which industrial action is considered illegal. Importantly, the list of enterprises that come under the heading of essential services is almost identical to that for ordinary public service enterprises, except that the Mint and broadcasting are not included and transportation services are more narrowly defined. It is also planned to drop banking (except for the Bank of Korea) and inner-city bus transportation from the list in 2001.

107. Under previous legislation, all public services were subject to compulsory arbitration. The ILO has repeatedly asked the Korean government to ensure that restrictions to the right to strike only apply to essential services in the “strict sense of the term”, under conditions of an “imminent threat to the life, personal safety or health of the whole or part of the population” (ILO 1996; 1998); the distinction in the 1997 legislation between ordinary and “essential” public services seems to be a partial attempt to respond to these concerns³⁹.

108. Other OECD countries also have provisions which ban or restrict labour disputes in the public sector or in industries defined as “essential services”. The idea that strikes in the public sector are different from those in the private sector and should be regulated differently, in particular to guarantee the continuous provision of certain services to the general public, is indeed reflected in the laws of many Member countries. However, there is no consensus view as to which public services are deemed to be “essential”, in which the right to strike is restricted, and those which are not. This is partly explained by the fact that the necessity for continuous provision of a service in any given country depends on a variety of geographical, economic and technological factors; an emergency in one country is not necessarily an emergency in another.

109. To mention a few examples among other OECD countries, in Austria and Germany there is a blanket ban on industrial action by civil servants (*Beamte*) which includes police, judges, and many teachers, social workers and employees in postal and railroad services (while other public employees under private-law contractual status are allowed to go on strike). In Spain, government can order compulsory arbitration to end a strike that involves “serious prejudice to the national economy”. Italy has laid down a list of essential services in its strike law which allow provincial prefects to uphold minimum services in public health, waste disposal, TV news, maritime links to the islands, and the payment of social security benefits (see Ozaki 1990; Jacobs 1998).

110. Korea is therefore not unique in restricting labour disputes in some public services. However, Korean labour law provisions seem to go farther than in other Member countries in that they set out an unusually broad definition of “essential services” where a strike ban covering entire sectors is maintained. Other countries have been more successful in pursuing alternative solutions, which help minimise intervention in freedom of association and the right to strike. These include the introduction of a “cooling-off period” in essential services, such as in Japan and the United States; the conclusion of voluntary no-strike agreements between management and unions in particular sectors; and regulations which, while allowing most employees of a particular industry to take industrial action, nevertheless require the maintenance of minimum or skeleton services. It should be noted that the Tripartite Commission has included the “adjustment of the scope of essential public services” on its agenda for future deliberations, albeit with no timetable to produce an agreed solution on this issue.

39. See the distinction between services considered as *essential* and *not essential* in ILO (1996, p. 112).

Payment of trade union officials

111. In contrast to previous established practice, the 1997 TULRAA prohibits the remuneration of full-time trade union officers by the employer, as well as any financial payment for regular trade union operations. This clause is supposed to take effect by the year 2002, when multiple trade unions will be allowed to co-exist at company level. The law has thus incorporated employer concerns that they will at that time be forced to support large numbers of paid full-time union officials from both FKTU- and KCTU-affiliated enterprise unions. Already under current conditions, employer associations complain that their members are forced to pay an unusually high number of union officers in relation to the workforce members they represent.⁴⁰

112. A survey of practices in other OECD countries shows that paid working time off for trade union representatives is not an uncommon feature of industrial relations systems. Additional time off for works council members (where these exist) is also widespread. In large enterprises, hours credits for both these functions often imply that many union officials devote their full time to union matters while being on the company payroll. In some countries, hours credits and time off for union officials are regulated in detail through labour law, while in other countries the matter is left to collective agreements.

113. To take one example, in France there are three major kinds of employee representation: the *délégués du personnel* (staff delegates), *délégués syndicaux* (trade union delegates) and members of the works council. All these representatives are guaranteed, by the Labour Code, a certain number of credit hours per month (varying by company size) to fulfil their functions. The number of delegates also increases with company size. More credit hours are available for work on health and safety issues, and for collective bargaining purposes. These hours can be cumulated and redistributed among delegates, and are also often extended by collective agreement, so that in fact there is a widespread practice of full-time trade union officials fully paid by their company (data do not permit the calculation of a ratio per workforce or union members).

114. In the United States, labour legislation aims to ensure that any payments for union officials are not for the purpose of interfering with or unduly influencing trade union activities, in which case they would constitute an unfair labour practice. However, payments to union officials, part-time or full-time, are allowed by law and court decisions if they are in the form of wages and benefits duly negotiated through collective bargaining, and do not restrict the union's ability to exercise its rights of freedom of association and collective bargaining. In fact, union officials are needed to administer the collective agreement and solve grievances that arise during its lifetime. Similarly, in Australia the 1996 Workplace Relations Act, while guaranteeing the workers' choice of bargaining agent, leaves the matter of payment of union officials to negotiations at company level. Only in Japan is this practice expressly outlawed through a clause in the Trade Union Act which prohibits employers to "give financial support in defraying the trade union's operational expenditures". In the view expressed on several occasions by the ILO's Committee on Freedom of Association, the prohibition of the payment of full-time union officials by employers is a matter which "should not be subject to legislative interference".

40. These include even officials working in national or sectoral union headquarters who usually maintain a formal employment relationship with their previous enterprise and continue to be on its payroll. The Ministry of Labour has published a figure of 6 600 full-time union officials, equal to a ratio of one official per 212 union members. The ratio of union representatives to all staff in unionised enterprises would be closer to 1:300 and, considering the low trade union density in Korea, the ratio to total dependent employment would be about 1:2000. There are no surveys or studies which would allow to compare these ratios with those in other OECD countries. Apart from the situation in France outlined in the text, a limited comparison may be provided by the German Works Constitution Act which requires the full release of one works council member per 300 to 900 staff, depending on firm size.

115. Among most recent developments, the Korean government has put a proposal before the National Assembly which would keep the prohibition of payment of full-time officials as a matter of principle, but would allow individual employers discretion to pay their union officials. However, strikes to enforce trade union demands in this matter would not be allowed, and a Presidential Decree would put a ceiling on the ratio of officials to union members.⁴¹

Union status of dismissed workers

116. The 1997 TULRAA specifies that an organisation will not be regarded as a trade union when persons who are not workers are allowed to join it. Accordingly, dismissed workers are not allowed to retain their membership in a trade union as soon as the dismissal has become valid (*i.e.* in case of a legal complaint of the dismissed worker, after the Labour Relations Commission and/or the courts have made their final decision). Although the February 1998 Tripartite Agreement did recognise unemployed workers' rights to join trade unions at sectoral and national (but not enterprise) level, a corresponding bill subsequently submitted by the government was rejected by the National Assembly. Despite repeated statements of intent by the government, no further bill has been submitted, as there seems to be disagreement among the Ministries concerned as to what type of unemployed might be allowed to join upper-level trade union organisations (in particular as concerns the length of their unemployment spell). As the KCTU experience has shown, the fact that some trade union officials are dismissed or unemployed workers, can lead to difficulties in securing legal recognition of a trade union by government authorities. If the law remains unchanged, this problem is bound to re-appear as new unions are formed and seek to register with government authorities.

117. This particular provision of Korean labour law has no counterpart in other OECD countries which consider qualification for membership as a matter for the union itself to decide and not to be set down in legislation. Most trade unions in OECD countries have varying proportions of students, self-employed, unemployed and retired workers among their ranks (OECD 1991, Chapter 4). For example, in Italy, the "gross" rate of trade union membership is about one third higher than the "net" rate which excludes all other categories but "employees in employment". United States and Canadian local unions tend to restrict eligibility to union office to members of the particular bargaining unit, although it would be rare that laid-off workers lose their membership, as long as they pay their union dues. However, these are practices decided by the trade unions themselves.⁴²

118. Similarly, in the Japanese system of enterprise bargaining, it is usually decided in the constitutional charter of each trade union, whether dismissed or laid-off workers can keep their status as union members. Up to the 1960s, Japan had provisions in its Public Corporations and National Labour Relations Law which disqualified those unions from collective bargaining which accepted as members, or

41. Current legislation already allows employers to give labour representatives time off for collective bargaining purposes or consultations within the Labour/Management Council. However, bargaining rounds only occur once a year and the law only allows for time off during that period. Similarly, works council members only get time off for attending, and preparing, works council meetings (usually four in a year). By contrast, in many enterprises grievances and new problem areas tend to arise continually during the course of a collective agreement, which would require the attention of worker representatives. For this reason, most OECD countries have institutionalised ways for the employees' voice to be heard on these issues.

42. Most OECD countries, including those characterised by enterprise-level bargaining, have at times experienced, or are still experiencing, high and often persistent unemployment, without using this as a justification for restricting the union membership of unemployed persons, even of the long-term unemployed.

elected as leaders, workers who were not employed by one of the public enterprises. After appeals to the ILO by the Japanese public sector trade unions, the Japanese government abolished these provisions and was then able to ratify ILO Convention 87 (Hanami 1985).

3. Arrest and imprisonment of trade union officials

119. Apart from the issue of labour law reform, the practice of arresting and imprisoning trade union leaders and members for violations of existing laws has also been a matter of considerable concern. Arrests of trade union demonstrators and officials have characterised the Korean industrial relations' scene throughout the 1990s. As shown in Table 2.4, numbers fluctuate considerably, as most are not detained for long -- however, some unionists, including high-ranking officials and even union presidents, have received substantial prison sentences. Charges tend to range from instigation of or participation in illegal strike action, to obstruction of business, violation of the National Security Act, breaking and entering and other forms of violence.

120. During the economic crisis of 1998 and 1999, many union members reacted strongly to the announcement of business restructuring and collective dismissals. This included takeover of plants and equipment, and strike action in essential services where the law prescribes conflict resolution through arbitration. In this context, arrests were particularly numerous, going up to almost 500 persons during 1998. At the end of 1998, petitions were made at the ILO on behalf of 141 workers subject to arrest procedures. Of these, only six seem to have remained under arrest as of June 1999; however, by that time, 70 more found themselves arrested or sought for arrest after new strikes and demonstrations. According to latest information as from February 2000, only three trade unionists remained under arrest, while seven were under indictment but free on bail, and one person was still sought for arrest.

121. The ILO's Committee on Freedom of Association has repeatedly urged the Korean government to take appropriate measures so that the persons detained or on trial as a result of their trade union activities are released or that the charges against them are dropped. The Korean authorities have argued that the concerned trade unionists had been arrested for violent acts or illegal strike action. They have also announced a long-range plan to "minimise" the number of arrests through focusing mainly on strike leaders and through applying fines, but not detaining other participants.⁴³

4. Current status and further perspectives of labour law reform

122. Substantial revisions of labour law have been undertaken since Korea joined the OECD in 1996. In several years from now, Korean labour law can be expected to guarantee labour rights to a similar extent as that prevailing in many other OECD countries. This should be the case, in particular, once trade union pluralism at enterprise level has been established, public servants have been allowed to join trade unions and bargain -- with all due restrictions pertaining to civil service -- about their terms of employment, and the government ceases to prescribe to trade unions who they should or should not accept as members. The step-by-step reduction of the list of "essential services" where compulsory arbitration applies, is also a move in the right direction. With these preconditions fulfilled, there should be no problem for Korea to sign and ratify ILO Conventions 87 and 98 on Freedom of Association and the Right to Collective Bargaining.

43. The ELSA Committee has taken the view that the definition of "unlawful activities" in Korea is very broad and encompasses union activities that would be regarded as lawful in most OECD countries (see the Report by the Chairman of the ELSA Committee to the OECD Council on Labour Law and Industrial Relations Reform in Korea, DEESA/ELSA/RD(99)3).

123. Solutions to the remaining problems need to be found to build up stability in Korean industrial relations and overcome the adversarial legacy characterised by an authoritarian management culture and trade union militancy. There are encouraging signs for a move away from past confrontational attitudes and for the emergence of new types of constructive and co-operative labour/management relations at workplace level. Not the least of these was the “concession-bargaining” of 1998, which saw trade unions prepared to bargain over wage restraint and even nominal and real wage reductions as an alternative to lay-offs and as a tool to overcome the economic crisis.

124. On the other hand, the repeated withdrawals by both labour and business representatives from the Tripartite Commission are not the right way to break out of the adversarial pattern and build up the necessary trust. It is hard to envisage how Korea will be able to construct a new industrial relations system without workable institutions like the Commission that accommodate the interests of the actors and enhance a climate of mutual respect among them. The Tripartite Commission, now endowed with legal status, has the potential to evolve into a core body for promoting social dialogue and social peace and for fostering a new, more co-operative climate.⁴⁴ However, it will probably take a considerable amount of time to overcome the legacy of distrust built up over past decades, as well as much good will on the part of government.

44. As the Korean government has noted, the Commission should “lead the nation-wide effort to resolve current economic hardships. [It] will continue to provide a forum for labour, management and government to work in co-operation for economic recovery and protection of workers’ rights” (MOFE, 1999, p.134).

CHAPTER 3

LABOUR MARKET PROGRAMMES AND THE PUBLIC EMPLOYMENT SERVICE

A. Introduction

125. As part of the response to the financial crisis, labour market programmes have been considerably expanded. The task has been especially challenging, in a country where the social safety-net was, at the start of the crisis, still in its infancy. Thus, the National Pension System was created in 1988 (and, as a result of its newness, it has not fully matured) and the Employment Insurance System was established in 1995. Even so, the government has managed to strengthen existing labour market programmes and to initiate new ones. A peculiar feature of these policies is that they have been supported by local governments, NGOs and indeed society at large. Thus, to a larger extent than in other OECD countries, local governments have adopted an active approach towards the unemployment problem. In 1998-1999, many of them extended or created their own employment offices that functioned in parallel with central government ones. They also reshuffled the administration and indeed many local civil servants have been asked to shift jobs in support of labour market programmes. Remarkably, to help finance these programmes, civil servants' wages were cut by 10 per cent in 1998.

126. Reflecting these efforts, government expenditures on "unemployment measures" have increased from negligible levels in 1997 to the equivalent of 2.2 per cent of GDP in 1998 and 3.2 per cent in 1999 (Table 3.1). Moreover, these figures under-estimate total public spending, as they do not take into account some of the employment programmes launched by local governments -- the cost of which was unknown at the time of writing. Given the improved economic situation and the falling unemployment rate, the prospect is for a lower expenditure on labour market programmes as a per cent of GDP.

127. Compared with other OECD countries, expenditure on labour market programmes appears to be highly sensitive to the cycle. During the crisis, it increased much faster than is the case in most other OECD countries facing similar economic circumstances. Table 3.2 shows patterns of expenditure on labour market programmes in different countries during periods of rapidly rising unemployment -- defined in the table as periods where the unemployment rate rose by over three percentage points. In the majority of the countries shown in the table, these expenditures grew by a few tenths of a percent of GDP. On the other hand, in Korea, as well as Finland, Sweden and, to a lesser extent, Australia, labour market expenditures have reacted strongly to the rise in unemployment. It can be argued that labour market programmes can be more effective in reducing the risk of long-term unemployment when they respond quickly and meaningfully to changes in labour market conditions, as has been the case in Korea.⁴⁵ It is also worth noting that the share in Korea of expenditures on active measures in total expenditure on labour market measures is 70 per cent (see bottom of Table 3.1), compared with about one third, on average, in the OECD area.⁴⁶ However, the actual effects of these programmes depend on specific characteristics of the programme design and implementation, notably the interaction between programmes and job-search

45. For a discussion of this issue, see OECD (1993, Chapter 2) and Calmfors (1994).

46. For a recent international study on this issue, see Martin (2000).

incentives, as well as the efficiency of public employment services in terms of programme delivery, which are examined in this chapter.

128. The purpose of this chapter is *a*) to examine the extent to which labour market programmes have adequately covered disadvantaged labour market groups, and *b*) to analyse the impact of the programmes on labour market outcomes. More specifically, it documents the expansion of labour market programmes in the face of the crisis, it identifies the strong and weak parts of the system and addresses its possible evolution. It starts with a brief description of the Employment Insurance System, which is the core pillar of government employment policies, as well as unemployment benefits (Section B). It then discusses active labour market programmes and their effectiveness (Section C). The chapter then reviews the functioning of a key institution in programme delivery, namely public employment services (Section D). It concludes with a preliminary assessment (Section E).

B. The Employment Insurance System and unemployment benefits

129. Together with the Industrial Accidents Compensation Insurance, Medical Insurance and the National Pension System, the Employment Insurance System (EIS) forms the basis of Korea's social protection system. The EIS was established in July 1995 as a comprehensive system intended to reduce the risk of unemployment, the risk of losing income as a result of unemployment and the risk of skill obsolescence.⁴⁷ Consequently, the EIS comprises three components, namely employment security, vocational training and unemployment benefits. The purpose of this section is to describe briefly the EIS and to examine the unemployment benefits component.

1. The Employment Insurance System (EIS)

A relatively limited scope of application

130. At the time of its creation, the EIS covered mainly regular workers in enterprises with over 30 workers (over 70 workers in the case of the employment security and vocational training components). Since then, the coverage has been expanded considerably in terms of both enterprises and types of workers that fall under the scheme. In January 1998, the system was expanded to cover firms of less than ten workers; in March 1998 to firms of more than five workers; since October 1998, it affects workers of all enterprises irrespective of their size. There remain important exceptions, however. In particular, the following workers are not covered by the EIS:⁴⁸

- part-timers working less than 18 hours a week or 80 hours a month;

47. According to Article 1 of the *Employment Insurance Act*, the purpose of the EIS is "to prevent unemployment, to promote employment, to develop and improve the vocational ability of workers, to strengthen the nation's vocational guidance and job placement capacity and to stabilise the livelihood of workers and promote their job-seeking activities, by granting necessary benefits when they are out of work, thereby contributing to economic and social development of the nation".

48. In addition, the employer should notify the relevant Employment Security Centre of any changes regarding both acquisition and loss of insurance of his/her employees. In the case of separation of a worker, the employer should submit to the Employment Security Centre a document that lays down the reasons for the separation. This is important, since a job loser is eligible to receive unemployment benefits only if separation is involuntary.

- daily workers who are employed less than one month;
- Government officials and employees subject to the Private School Teachers' Pension Act; and
- workers over age 65 and new employees over age 60.

131. Despite the recent strengthening of the system, only a relatively small proportion of the working population is insured. In July 1999, there were 12½ million paid workers, compared with a total of over 20 million employed individuals. This large gap is attributable to the fact that, as in other OECD countries, the system applies neither to the self-employed nor to unpaid family workers who, in the case of Korea, make for a disproportionate share of total employment. More importantly, only two-thirds of total paid workers are eligible under the EIS (this is so because many daily workers and part-timers are non-eligible) and only 70 per cent of those eligible are actually insured (Table 3.3). The coverage rate is low by international comparison. This can be explained by the fact that, as discussed earlier, the EIS covers a small proportion of the working population, and in addition, there would appear to be serious implementation problems. Aware of this problem, the government is considering measures to improve the coverage by the EIS of daily workers.

Funding of the EIS: a low level of social contributions

132. The EIS is funded by way of social contributions calculated as a proportion of the total wage.⁴⁹ There exist three different contributions, one for each component of the EIS: the contribution rate to the employment security component of the EIS is 0.3 per cent of the total wage; in the case of the vocational training component of the system, the contribution rate ranges from 0.1 per cent to 0.7 per cent of the total wage, depending on the size of the firm; a 1 per cent contribution rate has been set to finance the unemployment benefits component. While contributions to the employment security and training components of the EIS are borne by the employer only, half of the unemployment benefits contribution is paid by the employer and the other half by the employee. The three contributions together add up to 2 per cent, but authorities can bring the total contribution rate to a maximum of 3 per cent, depending on the economic circumstances.

133. Despite the low level of EIS contributions, it is somewhat surprising that the Employment Insurance Fund has maintained a surplus over the past two years. In 1998, the revenues to the Fund exceeded expenditures by about billion 170 won, or 12 per cent of the total Fund revenues. This is mainly due to the fact that many unemployed workers have not been entitled to receive unemployment benefits, thereby reducing pressures on the expenditure side. In addition, on the revenue side, the Fund has enjoyed a sizeable inflow of interest income, reflecting reserves accumulated in 1995-1997 -- a period characterised by a nearly full-employment situation. Excluding interest income, the Fund would have been in the red in both 1998 and 1999, thereby raising the issue of whether the EIS is adequately financed.⁵⁰

49. The total wage includes not just the basic wage but also all other elements of the remuneration such as bonuses and special allowances.

50. Though in principle both social contributions and benefits should be calculated on the basis of the basic daily wage, *i.e.* the total remuneration package, it is sometimes claimed that certain enterprises tend to pay contributions on the basis of the standard wage only. This could aggravate the funding problems of the EIS.

2. Unemployment benefits

134. The main role of unemployment benefits is to provide income support to workers who lose their job. At the same time, the system should encourage the re-employment of benefit recipients by making sure that they actively look for a job and remain employable. The Korean unemployment benefits system aims to meet both the income support and the re-employment objectives. It was established in 1995 as one component of the EIS, when the labour market situation was one of near full-employment. With the advent of the financial crisis, the coverage of the system has been widened and benefits have been made more generous, *i.e.* the income-support element is stronger. Despite these efforts, a relatively small number of the unemployed receive benefits while, for those who do receive them, the re-employment element of the system remains weak. These remaining problems are attributable to legal and practical difficulties regarding eligibility requirements, the rules that govern the duration and calculation of unemployment benefits and job-search enforcement mechanisms.

A relatively low proportion of workers eligible for benefits

135. In Korea, the main type of unemployment benefit is the job-seeking allowance. It is available to workers who contribute to the EIS, under certain rules and conditions. The other type of unemployment benefit is the employment promotion allowance. Its role is to encourage the early re-employment of recipients of the job-seeking allowance (see below).

136. The unemployment benefits component of the EIS has been designed to provide income support to job-losers -- new entrants are not covered. In addition, not all job-losers qualify for unemployment benefits under existing eligibility criteria:

- The claimant must be insured in the EIS for at least a *specified* period. The law provides that, as of 1 April 2000, the insured period should be no less than 180 days over the 18 months preceding the date of unemployment.⁵¹
- The claimant should be actively looking for a job. This implies that the claimant must register at an Employment Security Centre immediately upon separation and, when doing so, he/she should apply for a job.
- The loss of employment should not be motivated by a “serious fault” of the claimant. Neither should it reflect a personal choice of the claimant to leave the enterprise without justifiable reasons. Justifiable reasons include economic restructuring, the prospect that the company will suspend its operations or close down, the geographical transfer of the company and difficulties in adapting to new technologies.⁵²

137. It is important to note that a separated worker does not lose his/her entitlement to unemployment benefits if he/she receives retirement allowances upon separation. However, if retirement and other

51. Until 1-April 2000, the law provided that, to claim benefits, the unemployed had to be insured for at least 12 months over the 18 months preceding the date of unemployment. However, in the aftermath of the financial crisis, the requirement was relaxed significantly -- to claim unemployment benefits, the claimant had to be insured for at least six months over the year preceding the date he/she became unemployed.

52. The reasons for the separation must be specified in the document provided by the employer to the Employment Security Centre within a fortnight upon separation of the claimant. Apparently, the non-payment of wages for a certain period also provides a justifiable reason for leaving the enterprise and claiming unemployment benefits.

separation allowances granted by the enterprise exceed a certain amount, the payment of job-seeking benefits may be deferred by three months.

138. Although these criteria would not seem to be particularly strict, they effectively leave uncovered a large number of unemployed people. There are several reasons for this. *First*, new entrants, daily workers, part-timers and unpaid family workers are excluded, simply because they cannot be insured in the EIS. *Second*, even those workers who should be insured in principle may not be eligible to receive unemployment benefits when the employer does not transfer the social contributions to the fund set under the EIS. The non-payment of contributions is endemic among small businesses, which to some extent reflects the fact that the system has only been extended to these businesses recently and implementation inevitably occurs with a delay, particularly among small businesses that often ignore the law. But the non-payment of contributions might also be attributable to unwillingness on the part of these businesses to pay any taxes and social contributions. However, in order not to penalise the workers of those businesses, Employment Security Centres usually provide benefits to job-losers who meet all eligibility criteria except the non-payment of contributions by their employers. *Third*, there is significant turnover among certain categories of workers, notably those hired under temporary contracts. Therefore, some job-losers contribute for too short a period (less than six months) to qualify for unemployment benefits. *Fourth*, certain unemployed workers reportedly are not aware of the existence of the system and fail to claim their entitlements.

139. Reflecting the legal eligibility requirements as well as practical difficulties in increasing the coverage of the EIS, the proportion of unemployed workers who receive an unemployment benefit is very low. As of June 1999, about 170 000 unemployment benefit recipients were registered, that is 12½ per cent of total unemployment. In all other OECD countries for which data are available, the share of the unemployed that receive benefits is significantly larger -- in certain countries, almost all unemployed workers are granted an unemployment benefit.⁵³

140. In addition, certain categories of workers are more likely to receive benefits than others. Table 3.4 shows that during the first half of 1999, some 187 000 workers received unemployment benefits.⁵⁴ There is little variation in the benefit recipients/unemployment ratio by gender (even though the number of male benefit recipients was twice as high as that of female recipients, the figures are practically identical as a proportion of unemployment). By contrast, the benefit recipients/unemployment ratio varies significantly by age and level of education. In general, the proportion of older and more educated unemployed workers who receive benefits tends to be much higher than is the case of younger and less educated ones. Interestingly, despite the adoption of new legislation easing dismissal protection, less than 20 per cent of benefit recipients registered during the first half of 1999 had lost their job as a result of "urgent managerial reasons". Also, in about 10 per cent of the cases, the reason for job loss was either termination of the contract or worker's retirement and 7½ per cent of recipients were previously employed in a company facing bankruptcy.

53. Among the other OECD countries, in 1995 the ratio ranged from 27 per cent in Greece, 36 per cent in the United States and 39 per cent in Japan to 71 per cent in Switzerland, 94 per cent in Norway and to almost 150 per cent in Ireland (see Table 1.7 in OECD, 1998*b*). Reflecting methodological differences, these ratios are not strictly comparable across countries. However, they provide a useful indication of broad borders of magnitude and they highlight the internationally low beneficiaries/unemployment ratio of Korea.

54. This is a "flow" figure, which is therefore different from the number of unemployed at a point in time (stock concept). In the case of Korea, however, "stocks" come close to "flows". The reason for discussing in this paragraph "flows" instead of "stocks" is that the former can be disaggregated into different components, which is not possible in the latter case.

141. It is not possible to assess with any degree of accuracy the respective roles of the different factors that might explain the low coverage of benefits. It is possible, however, to infer that more than half of the unemployed workers do not receive benefits simply because they were not insured in the EIS prior to becoming unemployed. Available data suggest that out of the total number of workers that are insured in the EIS and lose their job for involuntary reasons, only about half qualify for unemployment benefits.

Level of benefits and duration of payment: an ungenerous system for low-wage workers

142. Not only is coverage limited by international standards, but in addition benefits are rather modest for the limited number of unemployed workers who receive them.

143. The (daily) job-seeking allowance amounts to 50 per cent of the so-called “basic daily wage” at the time of separation.⁵⁵ There is a certain risk that the basic daily wage at the time of separation is lower than the usual basic daily wage, the risk being especially high in the case of enterprises facing financial difficulties. Therefore, the law provides that the wage used as a basis for the calculation of the job-seeking allowance should be the “ordinary” wage, when the latter is greater than the basic daily wage at the time of separation. Importantly, the job-seeking allowance is not subject to taxes and social contributions. As a result, the net (after-tax) replacement rate, defined as benefits relative to expected income in work, exceeds 50 per cent. The privileged tax treatment of unemployment benefits may also have implications in terms of labour market incentives -- an issue addressed below.

144. The job-seeking allowance is subject to a ceiling and it cannot fall within a minimum level. The ceiling for the job-seeking allowance is set at 30 000 won per day, that is approximately \$25 a day or 56 per cent of the average daily wage.⁵⁶ Since January 2000, the minimum job-seeking allowance has been brought to 90 per cent of the minimum wage (up from 70 per cent before January) or about \$9.50.⁵⁷ The minimum job seeking allowance is now slightly above the minimum cost of living, which in December 1999 was officially estimated at 268 500 won per month, or 8 950 won per day.

145. The effective level of benefits depends on the insured wage at the time of job loss. Available data for 1999 show that the majority of the benefit recipients are low-wage workers. For about two-thirds of them, benefits were calculated on the basis of a wage below average. Conversely, only 21.2 per cent of them were entitled to the maximum benefit. On average, in 1999, the daily job seeking allowance amounted to 23 680 won.

146. The maximum duration of payment of unemployment benefits ranges between three and eight months, depending on the age at the time of job loss of the recipient and the period of contribution to the EIS (the insured period).⁵⁸

55. The basic daily wage includes all elements of remuneration, *i.e.* standard pay, bonuses, overtime pay, special allowances and any other type of remuneration, including in-kind payments. For the definition of the total wage, see Article 18 of the *Labour Standards Act*.

56. According to wage data published by the Ministry of Labour, the average wage was 1 599 000 won per month in 1999, or 53 300 won per day.

57. On the basis of the minimum wage in force between September 1999 and August 2000, *i.e.* 361 600 won per month or 12 800 won per day.

58. For example, recipients aged 30 to 50 at the time of job loss receive benefits during three months if the insured period is between six months and one year, four months if the insured period is one to three years, five months if the insured period is three to five years, six months if the insured period is five to ten years and seven months in the case the insured period exceeds ten years.

147. It is, however, possible for a job seeker to obtain an extension of the payment of benefits -- thereby lengthening the maximum duration of benefit payment. This possibility arises in three circumstances. *First*, the Employment Security Centre may decide to extend the payment of benefits for a period of up to two months to any qualified recipients who have exhausted their ordinary benefits and face particular difficulties in finding a job -- this is termed "individual extended benefit". The job-seeking allowance for recipients of the individual extended benefit is 70 per cent of the ordinary job-seeking allowance, *i.e.* 35 per cent of the basic daily wage at the time of separation. But this is subject to the same floor as in the case of the normal job-seeking allowance, *i.e.* 90 per cent of the minimum daily wage. *Second*, in special circumstances such as when unemployment increases markedly, the Minister of Labour can decide to provide unemployed recipients who have exhausted their benefits with "special extended benefits" for a period of up to two months. The level of the special extended benefit is calculated as in the case of the individual extended benefit and is therefore subject to the same floor. *Third*, a recipient who participates in a training programme on recommendation of the Employment Security Centre can receive 70 per cent of the job-seeking allowance until the end of the programme. The "training extended benefit" is paid for the entire duration of the training programme, with a limit of two years.

148. The law provides that the extended benefits should be offered only on exhaustion of the ordinary job-seeking allowance. Also, according to the law, a recipient cannot be granted different types of extended benefits simultaneously. But the extended benefits can be offered subsequently and in any particular order. Reflecting these rules, the maximum duration of payment of the job-seeking allowance, including the individual and special extension benefits, is ten months in the case of a recipient aged less than 30, 11 months in the case of prime-age recipients and 12 months for those older than 50. When the training extended benefit is taken into account, the maximum duration of benefit payment increases by two additional years.

149. The EIS was established in July 1995 and, therefore, in practice the maximum entitlement at present cannot exceed six months (seven months as of 1 July 2000), which combined with the individual extended benefits makes for a maximum of eight months (nine months as of 1 July 2000).⁵⁹ In addition, given that not all unemployed workers have been insured since 1995, the maximum is *de facto* much less for many recipients. Overall, in 1999, it is estimated that the average recipient has received benefits for about 98 days.⁶⁰ During the same period, taking into account that some of these recipients found a job before termination of their benefits, and that, on the contrary, other beneficiaries enjoyed an extension of the benefit payments going beyond their statutory entitlements, it is estimated that the average recipient has received benefits for 125 days (see KLI, 1999a).

150. An international comparison shows that, in most respects, benefits provided by the Korean unemployment insurance system are less generous than is the case in the majority of the other OECD countries where such benefits exist. The level of unemployment benefits is relatively low by international comparison. The statutory replacement rate is 50 per cent (or about 54 per cent when taking into account the fact that benefits are tax- and contribution-free in Korea), which together with the United States comes at the bottom of the OECD league table. In addition, benefits are subject to a relatively long waiting period of two weeks. Interestingly, however, the maximum level of the job-seeking allowance is relatively high and, conversely, the minimum is comparatively low by international comparison. In other words, compared with the systems prevailing in other countries, Korean unemployment benefits tend to be generous for high-wage job-losers and modest in the case of low-wage job-losers. The duration of benefits is shorter than is the case of the majority of OECD countries.

59. Authorities have decided not to provide special extended benefits in 2000.

60. This includes the two-month special extended benefit, which was awarded in 1999.

Job-search requirements and incentives

151. As in other countries, the system includes control mechanisms to verify that recipients effectively look for a job. There are also financial incentives in the case of early re-employment, *i.e.* when a job is found before expiration of benefits. Finally, the availability of other support systems also shapes labour market incentives. These schemes are described in Box 3.1.

Box 3.1 – Job-search requirements and re-employment incentives

The Korean Unemployment benefits system includes several “activation” elements with the purpose of encouraging the re-employment of benefits recipients. First, the system provides for the following job-search requirements:

- Job-seekers are encouraged to register at the Employment Security Centre as soon as they become unemployed.⁶¹
- In order to ensure that job-search and income support go hand-in-hand, a claimant who applies for unemployment benefits at the Employment Security Centre must simultaneously apply for a job.
- Every two weeks, unemployed recipients have to demonstrate to the Employment Security Centre that they are looking for a job. Failing this in any two-week period, the payment of benefits is suspended for the period in question -- though the recipient can obtain benefits in the following two-week period, provided the job-search requirement is fulfilled.⁶²
- The law includes the possibility of sanctions in cases where the recipient has fraudulently circumvented the job-search requirement. In this case, the payment of the benefit should not be made and the Employment Security Centre may request reimbursement of the benefit either in part or fully. Depending on the nature of the fraud, it may additionally impose a fine on the recipient amounting to up to one two-weekly benefit payment.
- The payment of unemployment benefit is suspended if the recipient rejects a job offer or a training programme recommended by the Employment Security Centre, unless there are justifiable causes for the refusal. These causes include cases where *a)* the job and/or training offer are inadequate vis-à-vis the skills of the worker; *b)* the offer entails a “difficult” geographical relocation of the residence of the worker; and *c)* the wage level of the offered job is “unreasonably” low with respect to market wages for the same occupation and area. The suspension of benefits lasts two weeks when a job offer is rejected and four weeks in the case of a training programme refusal. In other words, benefit entitlements are not lost entirely.

These requirements are not uncommon among OECD countries. Their effectiveness depends on how they are made operational by public employment services -- an issue treated in Section D.

Unemployment benefits also comprise a re-employment bonus, namely the employment promotion allowances. The purpose of these allowances is to encourage financially recipients of the job-seeking allowance to find a job before termination of the benefit period. There exist four such allowances. *First*, the early re-employment allowance can be paid to recipients of the job-seeking allowance who find a “stable” job before exhaustion of half of the job-seeking benefits to which they are entitled. The re-employment allowance amounts to half of the unused job-seeking benefits. In order to avoid possible abuse of the system and fraud, the re-employment allowance is provided on certain conditions, notably that the re-employed worker stays at least one year in the new job and that the new job is not located in the enterprise where he/she was last employed. The employer who hires the recipient of the re-employment allowance can in turn be granted a re-employment subsidy. *Second*, a vocational ability development allowance is available to recipients of the job-seeking allowance that participate in a training course on recommendation of the Employment Security Centre. *Third*, a wide area job-seeking allowance is available to recipients of the job seeking allowance who, following the suggestion of the Employment Security Centre, look for jobs in areas over 50 km from

61. Unemployment benefits are paid within 12 months upon the date of separation.

62. There exist, however, exceptions to the two-week interview requirement, notably in the case of illness and participation in training programmes.

their place of residence. The allowance is supposed to cover transportation and accommodation expenses incurred when prospecting in a wide area. *Fourth*, the Employment Security Centre may decide to provide a moving allowance to recipients who have to change their place of residence in order to either take up a new job or participate in a training course prescribed by the Centre. The amount of the allowance is supposed to cover the moving expenses and it therefore varies with the distance and the size of the recipient's household. In 1998, it was between 43 150 won and 348 790 won.

Despite their potential benefits, these schemes are not much used. For instance, only 17 318 recipients of the job-seeking allowance were granted the early re-employment allowance in 1998, and the figure for 1999 was 19 243.

Finally, a recipient who finds a job can keep part of the unemployment benefits. Indeed, the system includes a total earnings' disregard when the income earned is less than a certain threshold -- the latter is calculated as the difference between the daily wage at the time of separation and the daily job-seeking allowance. The earnings' disregard is partial when income earned ranges between the threshold and 80 per cent of the wage at the time of separation. Finally, when earnings exceed 80 per cent of the wage at the time of separation, the job-seeking allowance is lost. These rules apply to all types of income. Unfortunately, no data are available on the number of benefit recipients who have been allowed to keep part of their benefits while earning income from work. Experience from other OECD countries suggests that earnings' disregards can provide an important incentive mechanism for part-time work.

There is no systematic evaluation of the extent to which the activation elements of the unemployment benefits system discussed above contribute to increase re-employment probabilities. Available data show that one quarter of those who qualified for unemployment benefits between July 1998 and July 1999 managed to find a job during the same period.⁶³ It is not possible to draw from these data the fate of the remaining three-quarters -- they might remain unemployed or they might have dropped out of the labour market, but it is conceivable that some of them will have found a job in the unregistered economy.

152. It is safe to assert that the relatively low re-employment rate of benefit recipients is mainly due to the overall economic situation during most of the period analysed in this study. Indeed, there would seem to be relatively little risk of benefit dependency in Korea. For one thing, work is financially rewarding *vis-à-vis* benefits. The modest level of benefits (and their limited duration) provides a strong financial incentive for job-seekers to accept a job. In addition, under certain earnings conditions, recipients can continue to receive benefits when they accept. They can also be granted a re-employment allowance. The effects of the different benefits and incentive mechanisms are shown in Table 3.5. More fundamentally, work is highly valued from the social point of view. According to a recent attitudinal survey, three quarters of the unemployed would be prepared to accept a job entailing lower wages and working conditions than in the previous job (see Park, Y.B., 1999).

C. Active labour market policies

153. Active labour market policies (ALMPs) have attracted considerable attention among OECD policy makers. ALMPs are often regarded as a useful alternative to "passive" policies, especially in the face of high and persistent unemployment. They include a broad range of measures such as training; employment subsidies targeted to particular groups and direct job creation.⁶⁴ However, the

63. See KLI (1999a), Table 44.

64. The establishment of well-functioning institutions such as public employment services, with the aim of improving the matching between labour demand and supply, can also be regarded as an integral part of ALMPs. As in other labour market reviews, however, public employment services are reviewed separately in another section (see below).

cost-effectiveness of ALMPs needs careful evaluation; dead-weight losses, substitution and displacement effects may be quite high in many cases.⁶⁵

154. In Korea, given the relatively low levels of unemployment prevailing until recently, the focus on ALMPs is a new one -- except in the case of programmes for the employed. Most training schemes for the unemployed and direct job creation policies have been developed in the aftermath of the 1997 crisis to counteract the dramatic and sudden rise in joblessness. This section discusses the main features of these measures, leaving the role of public employment services to another section.

1. Training programmes

155. Training programmes can be instrumental in adapting or upgrading workers' skills, thereby enhancing their productivity and earnings. Korea has an established tradition in the area of training policies addressed to individuals in employment. These policies date back from the early 1950s, when the Korean government instituted centralised vocational training programmes to meet the requirements of the incipient industrial sector. By contrast, most training policies for the unemployed were introduced in the wake of the 1997 crisis.

Training programmes for the employed: a concentration in large firms

156. Korea suffers from under-provision of enterprise training, particularly among small enterprises. The system of training for the employed, which exists under the EIS, has helped improve the situation somewhat, but major problems remain.

157. The rapid economic development recorded since the 1960s and a shortage of skilled workers prompted the government to set up a training levy system in 1976. Firms were required to provide in-plant training or to pay a levy. After some initial success, the proportion of firms opting for training their workers, rather than paying the levy, fell steadily from over two-thirds of eligible firms during 1977-80 to less than one-fifth during 1991-93 (Table 3.6).⁶⁶ In 1995, a new training system was established as one component of the EIS.⁶⁷

158. The new system embraces different types of schemes targeted to employed workers (others, targeted to the unemployed, are discussed below) namely: *a*) subsidies to firms that conduct in-plant training; *b*) subsidies to firms that assign workers on paid leave for education and training; *c*) subsidies to firms for education and training courses that take place outside the firm premises; and *d*) subsidies to

65. For a more complete discussion see Martin (2000), and Betcherman *et al.* (1999).

66. Available studies suggest some success during the first years of implementation of the levy system, when there was a need for basic training (Jung, 1997, Kang, 1999 and Lee, 1999b). However, these studies also show that, during the 1980s and the 1990s, with the introduction of new technologies and the increasing complexity of the Korean economy, the levy system became inefficient. Reflecting ongoing technological change, the costs of conducting in-plant training grew rapidly, to the point that these costs exceeded the level of the levy by an estimated 30 to 40 per cent, thereby reducing the enterprises' incentive to train their workers (Jung, 1997). Most small firms opted for paying the levy rather than providing training. Overall, the levy system could not prevent under-provision of training while at the same time leading to waste of financial resources, as the system acted as a support mechanism in favour of firms that would have provided training in the absence of the levy.

67. The new, EIS-based system first applied to firms with over 70 workers and less than 1 000 workers, but since January 1999 it has been extended to all firms and the levy has been abolished.

employees for education and training, training for older workers and tuition loans. Data on expenditure and number of participants for the first half of 1999 show that, among the four programmes, in-plant vocational training is the most important one (Table 3.7). The programmes are financed by way of employers' contributions to the EIS, along the lines explained in Section B. The EIS supports 40 to 90 per cent of the cost of the training and, additionally, in the case of the paid leave scheme (see below), also one third to one half of the wage for courses that last over 30 days (Ministry of Labour, 1999a).

159. As shown in Table 3.6, the number of workers trained has increased since implementation of the new training policy under the EIS. In addition, most in-plant training schemes include "advanced" courses, instead of basic training as tended to be the case under the levy system (Korea Labour Institute, 1999b).

160. However, despite these encouraging results, it would appear that current training programmes for the employed suffer from certain deficiencies:

- Only a small proportion of the firms that pay contributions to the fund actually provide training for their workers. To take the example of in-plant training, which is the main programme, during the first half of 1999, less than 3 per cent of the insured firms provided in-plant training (Table 3.8, Panel A). During the same period, only 4.4 per cent of all insured workers received in-plant vocational training. The take-up of the other programmes of training for the employed is even lower -- for example, during the first half of 1999, about 1 400 workers were granted paid leave for training (Table 3.8, Panel B).⁶⁸
- Large firms are the main beneficiaries of the training programmes for the employed. As shown in Table 3.8 (Panel A), in the first half of 1999, the participation rate of firms with less than 150 workers in in-plant vocational training was negligible, while it exceeded 180 per cent in the case of firms with over 1 000 workers -- this high participation rate is explained by the fact that firms may claim support more than once over a given period of time. Only 1 per cent of those employed in small firms received in-plant training, compared with 12½ per cent in the case of large firms. Other programmes of training for the employed are mainly used by large firms.

161. It would therefore appear that training under the EIS has not succeeded in increasing substantially training provided by small enterprises. As large firms would, in any event, tend to train workers in the absence of specific policies, it seems highly likely that the training subsidies yield large "windfall" gains to large firms. Although the provision of training is likely to increase with the economic recovery, the system's effectiveness suffers from the excessive number of programmes and the fact that training tends to be concentrated in large enterprises. As in other OECD countries, there is a risk that workers in small firms, once trained, are hired by either another small firm or a bigger one. This risk may be higher in Korea, given the unusually large gap in terms of wages and working conditions between large and small firms (see Chapter 1). Future policies may consider introducing special financial incentives to encourage training by small firms and some targeting of the programmes at older workers, women and low-skilled workers.

Training policies for the unemployed: expansion, problems and possible reform avenues

162. Training programmes for the unemployed were considerably expanded during the crisis. The main training programmes available to the unemployed are *a*) re-employment training of the unemployed, a programme targeted to workers dismissed from enterprises covered by the EIS, independently of whether these workers are entitled to EIS unemployment benefits or not; *b*) training for employment promotion,

68. In the first half of 1999 tuition loans were given to almost 8 000 workers, predominantly males (66.9 per cent) and white-collar workers (85.5 per cent).

which focuses on dismissed workers, not previously insured at the EIS, *i.e.* mostly temporary, daily and part-time workers; *c*) training for the unemployed new entrants into the labour market (but most young unemployed have been granted internships under public work programmes, as discussed below); *d*) training for business start-ups, targeted at elderly unemployed, disabled individuals and school drop-outs; and *e*) manpower development training, which comprises initial training for craftsman and training for 3D jobs.⁶⁹ Of these, only the first programme is set up under the EIS and it is therefore funded from the EIS training fund. The others are financed out of the general government budget.

163. Remarkably, a large number of unemployed workers have participated in these programs. In 1998, 362 941 unemployed attended a training course and, during the first six months of 1999, the figure was 181 273 -- accounting for roughly one fifth of the unemployed in the period considered (see Table 3.9).

164. However, most programmes of training for the unemployed appear to be insufficiently targeted at disadvantaged labour market groups. Moreover, they tend to suffer from relatively high drop-out rates, while re-employment probabilities of those who complete the courses are low:

- Available evidence suggests that unemployed workers covered by the EIS are more likely to receive training than other unemployed individuals, and moreover, they receive a higher training allowance than other trainees. Almost half of all trainees in 1998, and 62 per cent in the first half of 1999, were trained under the EIS programme, *i.e.* re-employment for the unemployed (Table 3.9). The employment promotion programme was the next significant scheme, accounting for 28 per cent of the trainees in 1998 and 23 per cent in 1999, even though unemployed workers not covered by the EIS represent the majority of the unemployed. The unemployed trained under the EIS are given either the standard job seeking allowance⁷⁰ or a monthly training grant of 30 000 to 350 000 won (which includes allowances for transportation, family support and child care. Somewhat lower allowances are provided to participants to re-employment promotion training, while, under the other non-EIS programmes, trainees are paid a standard training allowance amounting to roughly 80 000 won per month.
- Slightly over half of the unemployed who undertook training courses in 1998 completed them within the same year (Table 3.9). Completion rates for 1999 are generally much lower, given the shorter observation period. An important reason for non-completion is dropping out from the course. The estimated drop-out rate for the first 6 months of 1999 is 23½ per cent (Kang, 1999). This might suggest some mismatch between the contents of the courses and labour market requirements -- indeed, the drop-out rate is very low in the case of training courses for 3-D jobs, for which there tend to be labour shortages and trainees have therefore a high probability of getting a job upon completion of the course. In addition, the fact that some trainees are not remunerated may have also played a role.
- The re-employment rate also tends to be relatively low, except in the case of training for 3-D jobs and for craftsmen (Table 3.9).⁷¹ Job-finding rates are the lowest for training for business start-up.

69. In addition, in 1998 there was training to return to agriculture, but this programme was abolished in 1999.

70. As explained in the previous section, recipients of unemployment benefits can be entitled to re-employment training that may last from one month to one year, until they find a job.

71. Re-employment rates are defined here as the proportion of the trainees that found employment after completion of (or during) the course (Kang, 1999). There is no clear indication of the length of time over which trainees are followed after completion of the course to determine whether they have found new employment. In some cases, either the institution that provided the course or the PES offices call up the trainees from time to time to check whether they have found a job. In other cases, trainees are supposed to inform the training providers or the PES offices about their employment situation.

- Evidence on the programme of re-employment training for the unemployed suggests that older workers are relatively less likely to receive training than other unemployed workers. Table 3.10 shows that a majority of programme participants are aged less than 29, while only 6 per cent are over 50. With respect to gender, men are more likely to participate in training programmes, though differences are not too large by international comparison.

165. In the absence of studies that compare re-employment rates with labour market outcomes of a control group (individuals with similar characteristics who did not participate in the programme), it is not possible to make a fully-fledged evaluation of the Korean training system. However, based on experience of other OECD countries, future reforms of the Korean training programmes could take into account a number of considerations. *First*, it is important to better target the programmes at disadvantaged labour market groups. Evaluation studies of training for the unemployed in different OECD countries have come to the conclusion that many programmes are not cost-effective, as returns in terms of increases in individuals' re-employment probabilities and earnings are not large enough to justify expenditures on the programmes. Well-targeted programmes, however, tend to be relatively successful. For instance, in the case of training for disadvantaged adult women, positive labour market outcomes seem to outweigh costs. *Second*, training courses are best targeted at those unemployed at risk of becoming long-term unemployed. According to Chapter 1, it appears that it is older workers that are more at risk of becoming long-term unemployed. Hence, targeting could focus on this group, if possible a few months after inception of their unemployment spell in an attempt to prevent them from entering long-term unemployment. *Third*, reforms of the programmes may perhaps improve on the matching of the unemployed to the content of training courses. In this respect, "training vouchers"⁷² may be an attractive solution, but only to the extent that vouchers are accompanied by professional guidance by the public employment offices in the selection of a suitable training course. *Fourth*, the design of training courses, and in particular their adequacy to labour market requirements, should be paid careful attention, as this is important to avoid inefficient expenditure on training. Finally, evaluation of the existing schemes in terms of total expenditure and labour market outcomes of participants relative to control groups should be conducted and repeated at regular intervals.

The delivery of training: an insufficient capacity to absorb the large inflow of trainees

166. It is often the same institutions that provide training for both the employed and the unemployed. There exist public training institutes (such as the Korean Manpower Agency (KOMA)⁷³ and other central and local government institutes) and private training institutions (*i.e.* in-plant training centres and authorised training institutes, usually run by NGOs). Since 1990, the number of public training institutions has increased only slightly, while, during the same period, the number of authorised training institutions

72. Training vouchers have been tested in a recent pilot experiment in Taejon, where trainees could use training vouchers to pay for training courses. 58 training institutes and 4 136 trainees have participated in the programme to date. The budget allocated to the programme in 1999 averaged 300 million won. Preliminary evaluation of the experiment indicates that the training voucher has met certain objectives, namely *a*) to give the trainees more freedom to choose which training courses to attend and at which training institutes, *b*) to simplify the administration of training and *c*) to collect electronic information on trainees and the courses they attended.

73. The KOMA, established in 1982, carries out a wide range of functions in the area of vocational training: planning and management of vocational training and of re-training for the unemployed; testing and registration of national technical qualifications; employment promotion; international co-operation and support to vocational training activities of developing countries.

rose by about 60 per cent and that of in-plant training institutions almost doubled. About 80 per cent of all training programmes for the employed and the unemployed are run by private training institutions.⁷⁴

167. Many courses run by private authorised training institutions are targeted at the “hard-to-place” unemployed and focus on providing basic skills. In particular, all training courses for women heads-of-household are run by NGOs under government sponsorship. The job-finding rate of trainees that completed these courses is estimated to be on the order of 40 per cent.

168. Public training institutions have suffered from the fact that the increase in the number of trainees has not been accompanied by a corresponding increase in staff members, so that the average number of trainees per instructor has increased considerably. As a result, the quality of training may have worsened. Future policies in this area should address this issue. In addition, the adequacy of training may benefit from more participation of employers and workers in the design of training programmes to make them more responsive to labour market requirements, as is the case for collective agreements on training existing in some OECD countries, such as Denmark and the Netherlands.

2. Employment maintenance and promotion programmes

169. A wide range of programmes for maintaining and promoting employment exist under the EIS and expenditure on these programmes has increased considerably in the wake of the 1997 crisis. Their aim is two-fold: *a)* to subsidise employment at firms that would otherwise lay off workers -- the so-called Employment-maintenance programmes. A situation that may require dismissals of workers must be recognised for the subsidies to apply;⁷⁵ and *b)* to promote hiring of certain disadvantaged categories of workers, such as laid-off workers, women and older workers, and also to encourage workers who take over their enterprise -- the so-called Employment-promotion programmes. An overview of these programmes is provided in Table 3.11. These programmes are financed by way of employers’ contributions to the EIS (see Section B). The level of subsidies is usually calculated as a proportion of the wage of the workers benefiting from the programme; but some employment-promotion subsidies are provided in the form of lump-sum payments. The subsidy is typically set lower for larger firms. The maximum duration of the subsidies was initially of 180 days, but it was increased to 200 days in 1999.

170. These programmes were especially useful in the face of the economic crisis. In 1998, almost 800 000 workers benefited from the programmes, that is about 6½ per cent of total dependent employment, and available data suggest similarly large numbers of programme participants in 1999 (Table 3.12). The programme addressing the temporary shut down of firms has been the most important one in terms of both the number of participants and, to a lesser, expenditures (Table 3.12). This programme may have contributed to maintain employment in firms encountering financial difficulties.

171. However, many of the programmes have not been much used, e.g. programmes aiming at maintaining employment by way of fewer working hours (Table 3.12). In addition, the rationale behind some of these programmes is difficult to understand. Also, it is unclear why the programme of training for

74. In particular, in 1998, private institutions ran almost all of the training for the unemployed not covered by the EIS, paid leave training and training for 3-D jobs; the KOMA ran all courses for craftsmen. Re-employment training for the unemployed covered by EIS was run mostly (68 per cent) by private institutions followed by the polytechnics, KOMA and the Chamber of Commerce. The Chamber of Commerce ran 66 per cent of training for business start-ups, followed by the polytechnics, KOMA and private institutions.

75. This is usually assessed in terms of increases in the level of inventories, a reduction in production, or measures taken towards restructuring and re-organisation of the firm (Ministry of Labour, 1999b).

employment maintenance is not administered as part of the general training programmes under the EIS. Moreover, employment promotion programmes do not sufficiently address the problems of disadvantaged groups. Expenditures on, and participation in, the programme for the re-employment of laid-off workers have tended to grow, while an opposite trend has been recorded in the case of the programme for the employment of women. Finally, employment stabilisation programmes tend to be biased in favour of large enterprises. Indeed, though it emerges from Table 3.13 that it is firms of size 30 to 300 that benefited more from the various employment subsidies in the first half of 1999, very large firms (above 1 000 employees) seem to be the ones that made most use of subsidies for unpaid leave of redundant workers. They are also those that benefited most from subsidies for childcare leave and for the establishment of in-house childcare facilities. Very small firms of size less than five are the largest users of subsidies for hiring laid-off workers and women.

172. Not much evaluation of employment stabilisation programmes is available to date. Some estimates of the net employment effects of the programmes, based on employers' subjective opinions, set at 22 per cent the overall net employment effect of the programmes (Kim, 1999). This is estimated to be larger for paid leave training programmes (29 per cent) and smaller for reduction of working hours (19 per cent). The estimated net effects are larger for small firms employing less than ten workers (33 per cent) and smaller for large firms employing 100 to 300 workers (17 per cent) and over 300 workers (19 per cent). This is suggestive of a better performance in terms of employment creation than that of similar programmes implemented in some other OECD countries whose net employment gains have sometimes been estimated at 10 per cent.⁷⁶

173. Future policy should consider reducing the number of programmes, enhancing their flexibility to respond to different labour market situations and simplifying the procedures to claim the subsidies. There is also urgent need for careful evaluation of the costs and benefits of the different programmes. Since they may worsen employment opportunities of workers not eligible such as youth new-entrants, possible substitution effects need to be evaluated carefully.

3. *Subsidies to small and medium size enterprises*⁷⁷

174. Small and medium-size enterprises account for a large proportion of employment in the Korean economy (see Chapter 1). The government has traditionally implemented a broad range of different policies to promote SMEs. These range from the provision of financial and technical support, to special taxation arrangements and to the setting of barriers to entry into sectors of economic activity reserved to small firms (see OECD, 2000a, for more details):

- Production lines reserved to SMEs were first established to promote SMEs' share in economic activity, and lately slowly reduced to improve macro-economic competitiveness. Production lines reserved to SMEs were 23 in 1979, 237 in 1989, and they are currently 88. The government plans to continue

76. In the experience of other OECD countries, such as Australia, Belgium, Ireland and the Netherlands, such programmes carry with them very high dead-weight losses and substitution effects. In particular, it has been estimated that dead-weight losses and substitution effects amount to some 90 per cent (Martin, 2000). It has been suggested that more targeting and monitoring of employer behaviour may raise the net employment effect of such programmes to 20-30 per cent, but at the price of stigmatising targeted workers.

77. It is sometimes argued that programmes targeted at SMEs undertake the function of countering market failures not in the labour market but in the capital or land markets (Betcherman *et al.*, 1999, p. 14). In light of this, it is usual to treat policies targeted at SMEs under competition and regulatory policies rather than under ALMPs, an exception being subsidies to the unemployed to start up their own business. The reader is referred to OECD (2000a) for a more detailed analysis of programmes for SMEs.

reducing the number of production lines reserved to SMEs to improve competition in the product market.

- In 1998, a total of 6.1 trillion won was spent to support about 30 000 SMEs with loans and grants by the Technology Credit Guarantee Fund (TGCF). Moreover, 45.7 billion won was allocated to support 983 venture firms by the Enterprise Promotion Fund for Software. The Fund for the Creation of Small Enterprises was started in 1999 to provide further support to small and medium size enterprises with a view to foster job creation; it provided 358.6 billion won loans to 2 873 firms (Ministry of Labour, 1999c, pages 15,16).
- A public fund of 100 billion won was set up to support the Korea Venture and Investment Fund Co-operative, with the aim of investing directly in venture enterprises and private sector venture capital. The activities of business incubators were supported, especially in terms of infrastructure such as business know-how and technology. In particular, the creation of firms in the cultural and tourism sector was promoted.

175. No information is available to date on the employment effects of these programmes. The restriction of some business lines to SMEs would appear to be against the interest of free competition and indeed recent policy initiatives go in the direction of progressively eliminating them. The provision of financial and technical support to SMEs is common to other OECD countries. However, in the case of Korea, the size of the support appears quite large and it is unclear whether this has helped SMEs become more competitive.

4. Public works programmes and internships

176. Public works programmes have been introduced in many OECD countries, usually with the aim of providing unemployed workers with professional experience, while reducing the risk of demoralisation, which is often associated with long unemployment spells. In Korea, public works programmes were set up in 1998. In principle, these programmes are targeted at the unemployed who do not have another source of income and are not entitled to unemployment insurance or training allowances. In addition, programme participants should be selected on the basis of certain criteria, including age, head of household status, number of dependants, house-ownership, assets, household income, gender, physical handicap, duration of unemployment and previous participation in public works. Public works appear to have covered a whole range of activities, from picking up cabbage to home-caring for the elderly and to PES job counselling. The programmes take place in stages of three-months duration. Individuals can take part in up to three consecutive stages, after which they can be selected again into public works only under special circumstances. An interval of a few days is provided between different stages of the project to allow participants to look for a job.

177. As far as the number of participants is concerned, public works programmes have been quite successful. About 440 000 individuals participated in the programmes in 1998, of which 100 000 in central government programmes and 340 000 in local government programmes. Participation in 1999 is estimated at about 780 000.

178. However, the implementation of the programmes has been criticised on different grounds:

- selection criteria for participation have been applied with some laxity. In contrast with the official targets, the incidence among total participants of well-educated individuals and prime-age workers has been relatively high (Table 3.14). In addition, women were less represented than men in the first stages of the programmes;

- some individuals have allegedly participated in a public works' programme while continuing to receive unemployment benefits or other public income support. Although these allegations could not be verified by the Secretariat, overlap with other labour market programmes is all the more conceivable that many actors are involved in the administration of public works. Indeed, as explained in Annex 1.1, several Ministries and many local government entities often run their own programmes;
- the funding of public works programmes introduces an element of unevenness in programme delivery across regions. Public works programmes are co-financed by three levels of government, namely central, provincial and district governments, based on a "matching fund system" (see Annex A for more details). But the co-financing rates of each government level vary from one region to the other;
- some displacement effects may have occurred, as wages under public works are in some cases higher than market wages for certain occupations in agriculture and 3-D jobs. The average daily wages of public works participants vary between 19 000 won, for basic skills work and 29 000 won, for professional and skilled jobs. This is much larger than the minimum wage, which is currently set at 12 800 won per day. In addition, it comes close to the average wage in occupations for unskilled workers, which is about 25 000 won per day.

179. These problems highlight the need for careful monitoring of public works. Controls on the use of the funds provided to local governments to run the programmes should be made tighter, while the targeting and remuneration of programmes should be improved so as to ensure that participants have an incentive to look for an un-subsidised job. Experience from other OECD countries shows that, unfortunately, these programmes rarely serve their stated purpose of improving re-employment prospects of participants in regular jobs. Generally, they seem to work better if targeted at the most disadvantaged groups (Martin, 2000 and Betcherman *et al.*, 1999). The Korean government is planning to gradually reduce public works in the future.

180. The programme of graduate internships is targeted at unemployed new graduates.⁷⁸ The aim of the programme is to provide college graduates with some practical work experience and to increase their employment chances in the light of the difficulties they face in the labour market. According to some estimates for 1999, re-employment probabilities of programme participants are on the order of 51 per cent (Ministry of Labour, 1999a). However, dead-weight losses are bound to be very large, underlining the need for an evaluation of the cost-effectiveness of this programme. It may also be important for future alternative policies in the area of graduate youth unemployment to assess which fields of studies carry with them higher re-employment probabilities.

5. Policies targeted at the disabled

181. There exist different training programmes for the disabled that are financed by the employment promotion fund for the disabled and general accounting funds. The average duration of these programmes ranges from six months to two years, depending on the type of disability. Participants receive a monthly allowance of 40 000 won, plus transport allowances (1 400 won per day) and food expenditure allowances

78. They last six months and the intern receives a grant of 500 000 won a month (400 000 in large companies) for a period of up to six months. Employers are supposed to pay interns some extra money in addition to this grant. Two phases of internships have been so far implemented, the first from December 1998 to August 1999 and the second from June 1999 to March 2000. Programme participants were 36 925 in the first phase and 8 337 to date in the second phase, for a total expenditure of 121.5 billion won. About 20 000 firms participated in the programme in each phase, over 70 per cent of which were small and medium-size enterprises (Ministry of Labour, 1999a).

(2 500 won per day). Between January and June 1998, 1 320 disabled individuals participated in the training programme organised by the Korean Employment Promotion Corporation for the Disabled, under the Ministry of Labour. Of these trainees, 73 per cent were men. Looking at the trainees' education level, 41 per cent were high school graduates; 20.3 per cent had a middle school diploma and 20.3 per cent had at most elementary schooling; the rest came from special schools or from college and university. The dominant age group was 15 to 30. Overall, the Korean government has made some worthwhile efforts to integrate disabled workers into the labour market. However, more remains to be done to promote employment and training of disabled women and disabled older workers.

D. Public and private employment services

182. In most OECD countries, many labour market programmes are administered by the public employment service (PES). The establishment of a well-functioning PES is therefore essential to their success. The extent to which unemployed workers will engage in job search, instead of relying on continued income support, depends on the activation strategies of PES officers.

183. In Korea, the PES has long played only a modest role in the job placement market. During industrialisation and in the tight labour market of the past decades, Korean companies have relied mainly on their own recruitment channels, in particular by placing newspaper advertisements, holding competitions among candidates or hiring relatives and other contacts of existing employees. Private employment agencies, which were legalised in the 1960s, have also been important players in job-search assistance and placement, particularly of low-skilled, but also more recently of highly-qualified personnel. However, a notable feature of the Korean response to the recent economic crisis has been the rapid expansion of the PES, in terms of both infrastructure and staff.

1. Quantitative indicators of job-brokering activities

184. Public employment services in Korea started after the Korean War, as industrialisation was about to get underway. At the time, the most important task consisted of assisting in the transformation of the excess labour supply in rural areas into an efficient urban industrial workforce. Around 50 employment offices were established around the country, operated by the Labour Ministry. The government also encouraged local governments to operate their own placement and counselling services, and by the mid-1990s, almost 300 offices were run mainly by municipalities. However, both types of PES suffered from lack of resources and staffing, with Ministry offices never reaching 1 000 staff nation-wide before the late 1990s (for a labour force rapidly approaching 20 million), and local governments seldom offering more than one or two job-search assistants in city halls. Private agencies filled the gap and tended to place many more workers per year into employment than the two types of public offices combined.

185. Available indicators suggest that the Korean PES occupy a relatively small share in the labour market intermediation process, compared to private employment agencies and also *vis-à-vis* the PES in other OECD countries. *First*, Table 3.15 gives a first indication of the relative importance of the three chains of employment offices outlined above. It is noticeable that there are four times as many private as public offices, although the Ministry of Labour has almost tripled its office network since the onset of the economic crisis, and municipalities provide additional placement services of their own.⁷⁹ By contrast, due to the quadrupling of the number of employees in the Ministry's offices, and a parallel increase in local government counsellors, the number of placement staff in public employment offices now probably

79. Apart from the local government offices listed in the table, many lower administrative units provide part-time "job counselling desks" which, however, cannot be regarded as full employment service offices.

surpasses that working in private agencies (detailed staff numbers of local government offices are not available). Nevertheless, even the over 3 000 staff in the Ministry's network represent a limited resource considering the size of the Korean labour force (see below for an international comparison of workload indicators).⁸⁰

186. *Second*, indicators of annual inflows of job-seeker registrations and notified vacancies and of annual placements, all as a percent of the labour force, illustrate the high market penetration of private agencies when compared with the national and local offices of the public employment service (Chart 3.2).⁸¹ The annual inflow of vacancies reported to public offices remained below 2 per cent of the labour force up to 1997 before increasing significantly with the expansion of the PES and the availability of public works administered by government authorities in 1998 and 1999.⁸² In comparison, annual vacancy inflows at PES offices in over a dozen countries reviewed by the OECD in the mid- to late 1990s have ranged from 3 to 14 per cent of the labour force, with the exception of Portugal and Switzerland (OECD 1996a; OECD 1999b). By contrast, the annual vacancy inflow in private employment agencies increased steadily from 3 to over 10 per cent of the labour force throughout the 1990s (reaching over 2 million in 1997), before falling back to 6 per cent during the economic crisis (*i.e.* at the same time as the inflow of vacancies in public offices started to grow). When comparing these data, it is important to keep in mind the different nature of vacancies at private and public agencies. In particular, private agencies are known for placing large numbers of low-skilled "daily workers" into short-term jobs, for example as housemaids or construction workers. PES-induced placements, while not all for permanent jobs, tend to be of longer duration.⁸³

80. As of 31 December 1999, the figure of 3 200 staff estimated to work for the public employment service under the Ministry of Labour includes about 2 550 staff working in local offices, additional personnel working on unemployment insurance in the Korea Welfare Corporation, as well as policy-making and supervisory staff in the Ministry of Labour and the Ministry's regional labour offices. This combined figure was estimated at 1 000 in 1995, with 850 staff working in local offices.

81. Three main data sets are important for a quantitative assessment of the job-broking function: the number of unemployed or other job seekers registered with employment offices; the number of vacancies notified to them; and the number of persons placed into jobs, *i.e.* the equivalent of vacancies filled. These data can be used to derive indicators of office performance and market share, such as notified vacancies as a proportion of registered unemployed, and PES-initiated placements as a proportion of registered vacancies or of total hirings in the economy. Various limitations of these administrative statistics need to be kept in mind, in particular when they are used for international comparison. It is well known that methods of collecting and classifying job vacancies differ from one country to another and that the extent to which unemployed persons register with labour offices depends on features of national legislation, particularly the rules on benefit payment. PES placements are also difficult to quantify. Countries differ as to what extent employment offices need to be involved for a placement to be recorded as "PES-induced". In addition, when an employment service tends to use fully-open vacancy displays, not all job hires that occur with PES help can be recorded as placements. Finally, a country's vacancy and placement data may be biased by over-representation of jobs with short duration. For these and other reasons, trends in performance indicators need to be interpreted with caution.

82. It is unusual that vacancy flows would increase at a time of recession. Available evidence suggests that the number of hirings in 1998 fell by almost half, compared to previous years. If vacancy inflows at PES offices, nevertheless, rose, this is probably due to the rapid increase of the number of PES offices and staff and to the publicity this entailed, to special efforts at vacancy acquisition and, to a limited extent, to the diversion of job offers which would previously have gone to private agencies. The availability of public works slots is likely to be another factor.

83. Chart 3.2 also illustrates the lack of incentives for unemployed persons to report to public offices before the start-up of the (un)employment insurance system (EIS), due to the lack of assistance expected and available from them in the past. Between 1989 and 1996, when the average stock of unemployed (as

187. *Third*, throughout the 1990s, private employment agencies in Korea have managed to fill over 80 per cent of their vacancies, as well as to place a similarly large share of their registered job seekers. By contrast, between 1989 and 1996, Ministry of Labour offices only succeeded in filling 15 per cent or less of all vacancies reported to them. This compares with vacancy filling ratios of over 50 per cent in most of the countries reviewed by the OECD where such data were available (Table 3.16). The proportion of vacancies filled by the Ministry's offices increased up to 50 per cent in 1998 and 1999 when, however, placements into public works projects need to be taken into account. Such projects did not exist before 1998, and it remains to be seen how the vacancy-filling ratio in PES offices will develop as public works are being scaled back or phased out in the post-crisis era.

188. *Fourth*, it usually is much harder for public offices to place their job seekers into jobs than it is for private agencies. For example, in 1997 it took the Ministry's offices about half a million referrals to fill 40 000 vacancies, and less than one fourth of all registered job seekers were placed into a job. By contrast, on average over 90 per cent of job-seeker referrals by private agencies are usually successful. Again, the different nature of jobs available at public and private offices needs to be taken into account. The high success rate of private agencies can at least partially be explained by the fact that such persons are placed several times a year and every short-term hire is counted as a placement.

189. *Fifth*, the share of vacancies notified to the PES in total hiring increased from 3 per cent in 1995 to 13 per cent in 1998, while the share of PES-induced placements in total hirings grew from 1 per cent in 1995 to 6 per cent in 1998 (Table 3.16). By these and other measures the market share of the PES in Korea has grown significantly in recent years, but is still lower than in almost all other OECD countries surveyed. For example, in various years in the mid-1990s, the share of PES-induced placements in economy-wide estimated hirings among the countries shown in the table ranged from 8 per cent in Ireland to 38 per cent in Germany.

190. *Sixth*, the low PES market share is confirmed by surveys enquiring about the job-finding channels used by recently hired wage and salary earners. According to a special survey, in 1998 less than 10 per cent of recent hires indicated that they had found employment through the PES channel. By contrast, over 45 per cent of the surveyed population had found work through recommendations or referrals by relatives, and the rest through newspapers and other advertising, recommendations by teachers, and other information available in schools and universities (Ministry of Labour, 1998a). Importantly, the share of new hires indicating use of the PES tends to decrease with educational level.

191. Client surveys show that many unemployed still lack confidence in the efficiency of PES staff and resources. For example, in the fall of 1998, over half of respondents in a survey taken by the Korea Labour Institute held negative views about the availability of suitable job openings at PES offices, the

measured by surveys) was about 400 000, *i.e.* between 2 and 3 per cent of the labour force, only between 60 000 and 90 000 in any given year ever registered as job seekers with the Ministry of Labour offices. Up to and including 1996, annual vacancy inflows at both Ministry and municipal offices were therefore superior to new job-seeker registrations, a situation quite unusual for OECD countries. This situation has now radically changed, as offices provide increased job-search assistance, unemployment benefits and a whole range of active labour market programmes. While the stock of unemployed (as measured by labour force surveys) has tripled after 1996 up to an annual average of over 6 per cent in 1999, the inflow of job-seeker registrations in PES offices has risen over twenty times during that period, to 9 per cent of the labour force in Ministry offices, and 6 per cent in local government offices. Many job seekers probably register in both Labour Ministry and municipal offices, but there seems less overlap between registrations at private and public offices.

speed of service provision and the adequacy of counselling on career development.⁸⁴ Although no comparable survey data exist for the employers' use of hiring channels, there seems little doubt that employers have relatively little confidence in PES efficiency, when it comes to hiring new staff. Particularly when recruiting higher-skilled personnel, employers are generally reluctant to use the PES and turn more readily to newspaper advertisements or private agencies, even if they have to pay for the services.

2. Placement and counselling activities in public employment offices

192. Previous OECD work has shown that an important institutional factor influencing the effectiveness of labour market policies is the degree of integration of the three core PES functions: *a*) job brokerage; *b*) unemployment benefit administration; and *c*) referral of the unemployed to ALMPs (OECD 1996*a*; OECD, 1997*b*). Only half of the OECD member countries currently have fully-integrated PES front-line offices. In Korea, to improve the complementarity between these core functions, placement and benefit departments which used to operate as separate parts of the local employment office, have recently been combined into an integrated "Employment Security Centre" which now offers a "one-stop service", handling all the classical tasks of a public employment service under one roof (the legal framework for employment services is explained in Annex 1.1). These tasks are, in particular: labour market information and analysis; registration of vacancies and job-seekers; job placement and counselling; job-search assistance through, for example, holding job-market fairs; registration of claims and payment of unemployment benefits; administration of subsidies to job seekers and employers and referral to training and public works programmes.

193. In the future, it is planned that job seekers will also profit from a more intensive "profiling" service, by which they are classified at the moment of registration according to their need for more or less intensive job-search assistance.

Office resources: the coexistence of different networks

194. As noted above, the Ministry of Labour has substantially increased the number of its PES offices and available staff during the recent economic crisis, to respond to the growing inflow of unemployed job seekers. As of December 1999, underneath the 46 regional labour offices there were 122 "one-stop" Employment Security Centres in operation, as well as 20 "Manpower Banks". The latter handle placement, but not benefit administration, and tend to specialise in services for higher-skilled job seekers, although this may vary from office to office. The Ministry also manages over a dozen placement centres targeted at daily workers.

195. In addition, practically every municipality and local government have established employment services of their own, which have also been provided with increased staffing during the crisis. The local "job information centres" offer placement assistance and counselling and refer clients to training places and public works; however, they do not pay out unemployment benefit and do not perform eligibility checks. Job seekers may register both at national and local offices, and employers may also report their vacancies to both, so that there is some degree of overlap between office activities. Placement offices in local government are more numerous than those under the responsibility of the Ministry of Labour. Korea is unique among OECD countries in this respect.

84. Only 10 per cent partially or totally agreed when asked whether "job-openings suggested were adequate", and only 21 per cent agreed that the offices "provided services quickly". By contrast, almost three out of four respondents agreed that "staff were kind and friendly" (Keum, 1999).

Workload of PES staff

196. To provide a comparison of office networks and staff workload with other OECD countries (where the involvement of local government in job-brokering is much less widespread), the analysis below focuses mainly on the office structure under the Ministry.

197. First, Table 3.17 provides information about the density of the network of Ministry's PES offices in Korea and nine other OECD countries. With the exception of Sweden, the latter are all countries with a fully integrated PES that, like in Korea, combines all three core functions.⁸⁵ The geographical area covered by a local office, still comparatively large in 1995, is now less than in many other OECD countries. However, due to Korea's high population density, an average Ministry's PES office still services a higher proportion of the population and labour force than in the other countries shown in the table, in particular the Nordic countries with their highly decentralised office network. The exception is Germany, which has large office districts covering on average over 400 000 inhabitants.⁸⁶ The average size of a Ministry's PES office in Korea has tended to be small, which is in harmony with the trend in most other OECD countries, where small offices are seen as more efficient to respond to local labour market conditions and opportunities.

198. Chart 3.3 shows the resource intensity of the Ministry's PES offices as measured by the average workload per PES employee, using various stock and flow indicators. Whether one regards the total labour force or the number of wage and salary earners as the potential clientele of the PES, the Chart shows that on these indicators the Korean PES is less well resourced than its counterparts in the other countries shown, although the ratios improved considerably since 1995.

199. When reviewing Table 3.17 and Chart 3.3 it should be kept in mind that the actual number of staff working on PES-related tasks is currently much higher than the 3 200 staff shown, due to the flexible response of local governments to the crisis which transferred hundreds, perhaps thousands of their staff to employment services. If the local government offices were added (although there is territorial overlap with Ministry offices) the average area of a district and the average population and labour force served per office would show Korea as closer to the average for other OECD countries.

200. A more realistic measure of workload may be stocks and flows of job seekers and vacancies that a counsellor has, on average, to deal with. It should be kept in mind that these indicators are influenced by the conjunctural situation and are shown only for a single year (with the exception of Korea). The international comparison may also be biased by the varying proportions of PES staff that actually process vacancies or come into contact with job seekers.⁸⁷ In Korea in 1999, there was an average monthly inflow onto the register of 47 job seekers per PES officer, more than in all other countries shown, apart from Spain (the OECD country with the highest unemployment rate). One officer had, on average, 20 new vacancies available per month to help place his applicants, similar to the situation in Japan. The current 2:1 ratio between new job seeker registrations and newly available vacancies per PES official is roughly similar to that prevailing, for example, in Austria, Germany and Sweden.

85. In Sweden, the payment of unemployment benefit is not integrated in the PES.

86. However, German PES offices usually have several decentralised "auxiliary offices" which assume part of the workload.

87. Varying proportions of PES staff work in local (as compared to regional and national) offices; and varying proportions are involved in chores not related to placement or job matching activities.

The precarious employment status and inadequate qualifications of new PES staff

201. The expansion of national (*i.e.* Ministry-run) PES staff during the economic crisis has relied mainly on the hiring of salaried job counsellors who work under time-limited contracts of mostly one-year duration. By contrast, before 1998, the large majority of staff were full-fledged civil servants. A fluctuating number of employees are even hired under “daily worker” contracts, in particular to examine unemployment insurance eligibility (Choi, 1999). About two out of three staff are now salaried employees. These are mostly recent college graduates with computer skills, but no counselling experience. They are recruited on the open job market, while civil servants undergo the usual civil service entrance examination.

202. The precarious status of the salaried job counsellors, as well as the legal restrictions for contract renewal, make it difficult for employment offices to retain these staff over the long term. The situation is also not conducive to investment in job training, although the Labour Ministry runs its own training centre and in theory all counsellors should receive training in job-counselling methodology, labour law and the processing of unemployment benefit claims. For civil servants, the custom of frequent transfers between posts, while it does not seem favourable to long-term specialisation, may facilitate rotation of staff between the core PES functions as outlined above.⁸⁸

203. In expanding their own employment services, municipalities and other local governments have either transferred personnel from other departments or are relying on public works posts. Either way, staff has relatively little specific expertise in placement and counselling, which is problematic given the nature of the tasks they perform (Box 3.2). There is also considerable turnover, particularly among public works personnel. It seems, therefore, that both types of public offices could benefit from a higher degree of employment stability.

Box 3.2 – Selected activities of the Korean PES

Job-seeker registration and follow-up

Job-seeker contacts with the PES start with registration. Employed job seekers and unemployed persons not eligible for benefit fill out a job-application form, which remains valid for three months. Job-losers who want to claim unemployment benefit, have to register with an Employment Security Centre within 15 days upon dismissal; they fill out both a job application and a benefit application form. During the registration process, the office classifies the job seeker into one of different categories with a view to re-employment probabilities -- a rudimentary form of profiling which is envisaged to be more fully introduced in the PES system over the coming years. In principle, this job-seeker

88. Office staff is usually divided into separate divisions for placement, benefit and vocational training (“job ability development”). Counters for customer service also tend to be separated by function, although in some centres the same counsellor may handle registration for job search and for unemployment benefit. In the recently established Kangnam Employment Security Centre, for example, 36 staff are working in three divisions: 12 staff in the employment assistance team dealing with counselling, placement and job subsidies (five civil servants, seven salaried job counsellors); 16 staff in the employment insurance team (six civil servants and ten salaried counsellors); and eight staff in the job ability development team which deals with training referrals and counselling (six civil servants, two salaried counsellors). If this distribution of staff is indicative of the PES overall, the insurance department would take up the largest share (close to half) of personnel resources. While the numerical predominance of benefit staff is also characteristic of a few other OECD countries, many countries are making efforts to keep the share of their placement and counselling staff at a comparatively higher level. Previous OECD reviews found, for example, that in Austria 54 per cent of staff was working in “service” departments, providing job-broking and vocational guidance, while 29 per cent were in benefit departments and 17 per cent in other administration. In Sweden, when staff working in the so-called “unemployment insurance funds” are taken as part of the PES, they constitute less than 25 per cent of all PES employees. By contrast, in Belgium employees working on benefit payment are about half of total staff (OECD, 1996c; 1997c).

classification should be made on the basis of a comprehensive interview, but interviews have tended to be quite short recently due to the large influx of job seekers during the economic crisis.

The employment insurance department subsequently contacts the applicant's last employer to find out the reasons for job loss and checks the person's contribution record in order to decide on benefit eligibility. To receive confirmation of their status as an unemployed benefit recipient, job seekers need to visit the PES office every two weeks after registration and demonstrate proof of job-search activities during the period in question.⁸⁹ Counsellors are supposed to verify the exactitude of job-search records by contacting companies, but are hampered by insufficient staff.

After their benefit eligibility is established, the unemployed are often asked to participate in collective information sessions on office premises. A kind of "job club" has also been started, intended to develop a greater degree of autonomy on the part of job seekers by preparing them for self-employment or business start-ups, or teaching them more efficient job search techniques. In the past, there has been very little long-term unemployment beyond a duration of six or even 12 months. Consequently, there is little formal regulation concerning a more intensive, personalised follow-up of long-term unemployed persons such as the job-guidance or back-to-work plans which have, over the years, been developed in other OECD countries. However, counsellors do keep electronic interview records as a basis for more intensive job seeker follow up over time.

Handling of Vacancies

In many countries, it is a priority task of the PES to increase the number of vacancies received. In Korea, in the past, the great majority of vacancies were not notified to the PES, which can be attributed to the entrenched custom of recruitment through personal connections, and to employers' low assessment of the PES staff's ability to screen applicants.

As in other OECD countries, Korean offices have now started to search actively for vacancies by visiting employers. Otherwise, employers will report vacancies by phone or come to the office to fill out the necessary forms and describe their detailed needs. Many employers will notify their vacancies to both national and local government offices.

Job information to be given by the employer includes basic working conditions such as pay (regular and bonus), working hours and contract status. The desired gender⁹⁰, age and education level of the future jobholder, as well as the number of staff and the presence of union representation within the firm also tend to be indicated. PES counsellors may negotiate with the employer on the various ways of advertising a vacancy. The latter will have the final choice as to whether to treat it as an "open" vacancy where full details of the job are advertised on bulletin boards and on the PES electronic information system; as a "semi-open" vacancy, where the applicant needs to contact a counsellor to get full information; or as a "closed" vacancy, where the counsellor decides not to advertise widely the vacancy, but instead pre-selects a certain number of candidates to refer to the employer.

It seems that up to now, PES offices have preferred open vacancies without much intervention of staff, as screening and pre-selection of applicants through in-depth interviews were limited by the small number of office personnel. The great majority of vacancies are made available to office clients through bulletin boards and self-service terminals, and also to the general public through the PES Internet site. Currently, vacancies put on the web usually include the full address of the prospective employer.

This may change as a result of high unemployment and slowly emerging long-term unemployment, which tend to increase the need for personal follow-up and targeted job referrals of the hard-to-place. With high unemployment, semi-open and closed vacancies would seem to be more effective to place workers with employment handicaps. However, when opting for a strategy of referring pre-selected candidates, the employment service needs to be aware

89. Current regulations require demonstration of at least one job search effort during the period.

90. The indication by employers of the desired gender of job applicants, which is openly posted on vacancy notices in many PES offices, may be somewhat surprising in view of Korea's Equal Employment Act under which employers are held to avoid use of criteria not related to job performance, such as appearance, height or marital status.

that employers who find that too many referred job seekers are not genuinely interested in a job offer, become reluctant to notify vacancies to the PES (OECD, 1996a).

In the case of semi-open and closed vacancies, counsellors have the option to limit job referrals to the vicinity or commuting area. The administrative guide for placement services recommends that this be done; however, if no appropriate vacancies are found in the commuting area, nation-wide search and referrals are available.

Special placement assistance is given to companies suffering from labour shortages; for example, special office personnel is handling vacancies for the so-called 3-D jobs (*dirty, difficult and dangerous*) which are not easily filled, mainly due to the rising education level of the Korean workforce and the accompanying job aspirations.

Job matching and job referral practices

The computerised *Worknet* system is the primary tool for the matching of vacancies and job seekers. This is regularly done by job counsellors with the help of the information provided by employers and job seekers on their respective registration forms. In addition, job-aptitude tests may help counsellors to steer applicants to the most appropriate vacancies. Many clients will also do their own matching operations by using the self-service terminals available in PES offices (both under the Ministry and local government). Two search functions are available: one for job seekers looking for vacancies and one for employers looking for suitable candidates.

A good occupational classification system is the foundation for efficient matching, and the Korean PES is currently developing a new matrix, fine-tuning the occupational classification and allowing for skills overlapping across different occupations. The diffusion of the Internet has created new opportunities for job matching: the availability of vacancies and job seekers can be posted on the web and will, upon inspection by the labour office, be integrated in the *Worknet* information system which, again, is distributed via the worldwide web. Applicants may give their full name and address for inclusion in the *Worknet* and can thus be contacted directly by an interested employer. Nevertheless, in most cases only the applicant's last name, but not his address, is made available on the PES web site.

The modern computerised forms of self-service without the mediation of the employment office may also be a reason for relatively low PES-induced placement shares in Korea, as the office may not have a record of who used its services. However, this problem is not unique to Korea; several PES agencies in OECD countries have now discontinued giving PES-induced placement numbers and ratios.

When potential applicants for a position have been identified through matching, or have approached a counsellor themselves in the case of a semi-open vacancy, candidates are usually sent to a prospective employer with a letter of referral, asking the employer to report back the results of each specific interview. About 60 to 80 per cent of employers usually do report results, quite a substantial amount. PES offices also provide for separate interview rooms for meetings between job seekers and employers.

Notification of collective dismissals to the PES

The PES may become involved in collective dismissals by receiving notification of anticipated dismissal above a certain size. This requirement, already contained in the *Employment Security Act*, was further defined in the *Labour Standards Act*, as revised after the February 1998 agreement in the Tripartite Commission (see Chapter 2 for details). In these cases, the local PES office or the regional labour administration may participate in negotiations on the dismissals within the enterprise, or point out the range of available subsidies for avoiding any layoffs, such as work-sharing or employment maintenance subsidies.

3. Placement activities by private employment agencies

204. The Korean PES has never enjoyed the "placement monopoly" characteristic in the past of many OECD countries, as private employment agencies have existed for many years -- there are currently almost 1800 of them -- and have a market share superior to that of public services. For many years up to 1998, private agencies accounted for over 90 per cent of all registered placements in Korea. By contrast,

temporary work agencies have only become fully permitted through the 1998 Tripartite Agreement and the subsequent *Act on Dispatched Workers*.

205. As noted earlier, private employment agencies have been able to capture a relatively large market share for several reasons. First, public services have long had comparatively little resources. In addition, the private agencies specialise in types of jobs which the PES has given little attention to in the past, in particular to managers, professionals and skilled specialists at the upper end, and to unskilled workers, such as housemaids, waiters and construction workers, at the lower end of the market. Only recently has the PES provided competition at the upper end, by focussing on high-skilled labour in some Manpower Banks. However, the high market share of private agencies in placements is mainly due to their focus on short-term and daily jobs. For example, of all placements by one private agency in Incheon over the last seven years, only 5 per cent consisted of placements into permanent employment.

206. The Employment Security Act regulates the operations of private employment agencies. Free private placement services, such as those operated by trade unions, employer associations or non-profit organisations, were always allowed to operate with little administrative restriction. By contrast, fee-charging agencies used to operate under more important restrictions, which have only been lifted in early 1999. Since then, new agencies have no longer to apply for a three-year permit and can start operating simply by registering in writing with the competent government office. In addition, reporting requirements were relaxed, most limitations on job categories where private agencies can operate were removed, and rules specifying material details such as the size of office space were lifted.

207. The Ministry of Labour has also relaxed to some extent the restrictions on the size of fees, which private agencies can charge. In contrast to most OECD countries, a practice has developed where private agencies may collect fees from both employers and job applicants. The Ministry has fixed the upper limit of the job applicant's fee at 40 per cent of the fee asked from employers.⁹¹

208. As outlined in Chapter 2, a 1998 *Act on Dispatched Workers* has set the framework for the use of temporary work contracts. This act legalised a practice that was already widespread before. Temporary workers tend to be less skilled, often production workers or office clerks. In contrast to private placement agencies, temporary work (or "dispatching") agencies still need permission to operate and are subject to restrictions in terms of the range of occupations, types of work and length of contract. Agencies are also required to pay regular employment insurance contributions for their dispatched workers. They are not allowed to hire out workers to firms where industrial disputes are taking place, and usually need to wait two years before replacing workers dismissed for managerial reasons (redundancy). Outside of the 26 specific occupations detailed by Presidential Decree, where a two-year limit on overall duration applies, the hiring-out period is restricted to three months duration, renewable only once.

209. As in other OECD countries, the law makes a clear distinction between such temporary work agencies and offices for private placement. In particular, there needs to be a triangular contractual relationship between the dispatching agency, the temporary worker, and the user firm. When hiring out a worker to a user enterprise, the agency maintains a contractual relationship with the person; a private placement agency, by contrast, has no such relationship with a worker who found employment through its services.

210. For this reason, there is little overlap between the two types of offices. Compared with placements by private agencies, the number of referrals by TWAs is still relatively low; in mid-1999, some

91. The legal possibility for charging fees to job applicants seems to conflict with the ILO's Convention 181 of 1997 (not signed by Korea) which specifies that "private employment agencies shall not charge directly or indirectly, in whole or in part, any fees or costs to workers."

46 000 workers were hired out from about 800 registered “dispatching” agencies, a share of 0.4 per cent in dependent employment. According to 1999 survey data, almost half of these workers were hired out for periods over nine months, which implies that employers tend to substitute them for regular workers instead of using them for short, intermittent work. Their average wages were barely above 50 per cent of the Korean national average (Jeong, 1999).

211. The extent of private sector involvement in placement which is characteristic of Korea is useful for the debate in OECD countries about the role of private employment services and public/private contestability. The dominant trend in OECD countries has been to liberalise employment services, end the public sector monopoly in placement (where it existed) and allow for stronger private competition. In Korea, it has already been possible for many years to challenge (“contest”) public employment services in the area of job placement, and private training providers have long competed with public sector training institutes. Nevertheless, as outlined, competition in placement has remained limited as both office types have tended to service different clients. Competition has recently increased as the PES was expanded during the economic crisis.

212. There are currently no notable links between PES offices, on the one hand, and private employment or temporary work agencies, on the other, apart from the fact that the latter can use the openly available *Worknet* files. This may be considered somewhat surprising, as the government could have decided to make use of the extensive network of private agencies to *stimulate* competition between public and private providers, for example through payment of fees to private agencies for placing unemployed job-seekers, instead of relying solely on its own services. Examples of this type of “contestability” exist, *inter alia*, in the Netherlands, Switzerland and Australia.

213. The most radical reform of the delivery of labour market assistance through emphasis on private providers has been underway in Australia. Under the Australian “case-management” system, private, community and public sector organisations are contracted as providers of employment services under a market-oriented approach. Public providers operate under the same conditions (regarding tendering, fees for successful placements, etc.) as private providers. The role of the Ministry (the Department of Employment, Education, Training and Youth Affairs -- DEETYA) is to purchase employment services on behalf of job-seekers, and to manage the tendering and contracting process, while ensuring that service delivery is subject to contestability by public, private and community providers (OECD, 1997*b*; Fay, 1997).

214. In the mid-1990s, the Swiss cantonal labour office in St. Gallen, in the face of rising unemployment, started to commission private employment agencies to place unemployed workers registered with the PES. These agencies spend on average more time on placement efforts than the public offices could afford (OECD, 199*b*). In the Netherlands, the PES has since the early 1990s paid a subsidy to TWAs which take the long-term unemployed on their payrolls. It has also become active itself in the market for temporary work by creating a joint venture with two other TWAs (inforMISEP, 1999). On the basis of the 1996 Employment Act, unemployment benefit institutions (which do not form part of the PES in the Netherlands) and social assistance offices can, as in the Australian example, “buy” reintegration services from either public or private providers.

215. The Korean authorities would do well to consider these examples of stimulating private sector initiatives in the area of job placement as a possible alternative to further expanding their own placement services and as a possible boost to the effectiveness of back-to-work programmes. The aim to increase PES market share may ultimately be less important than innovative strategies to speed up and facilitate the reintegration of unemployed job-seekers into the labour market.

E. Assessment

216. Labour market programmes have to be evaluated in the light of their twin objectives, namely *a)* to provide income support in the face of rising unemployment and *b)* to encourage the re-employment of unemployed workers, while minimising the dead-weight, substitution and displacements effects often associated with such policies.

217. Regarding the first objective, the portfolio of labour market programmes has been expanded considerably in the past two years. However, it is officially estimated that, out of the 1.5 million individuals unemployed in 1999, only 61 per cent participated in one of the various labour market programmes (Chart 3.1). The remaining 39 per cent were potential clients for social assistance benefits (discussed in Chapter 4). Only 29 per cent of all unemployed workers received benefits from the EIS, in the form of either unemployment benefits, training or employment security schemes. Almost one quarter were engaged in public work programmes and 9 per cent participated in the other non-institutionalised schemes, *i.e.* unemployment loans and internship programmes. In addition, training programmes for the employed have not succeeded in increasing the provision of training on the part of SMEs.

218. As to the labour market effects of labour market programmes, in the absence of any systematic evaluations it is not possible to draw clear-cut conclusions. However, based on the examination of specific design features of the programmes, the following observations can be made. *First*, there is a general lack of targeting in many of the programmes. As a result, it is unclear whether they really reach disadvantaged groups identified in Chapter 1, such as unemployed workers not covered by the EIS and older workers. Targeting is especially important in the case of subsidies to SMEs, given that this programme is the largest in terms of government spending on ALMPs. *Second*, despite a general lack of targeting, some of the programmes are not much used. This suggests that some regrouping of programmes may be called for, notably in the area of employment maintenance subsidies. *Third*, in a context of much brighter economic prospects, there is a case for reducing substantially the scale of public works programmes. International evidence suggests that these programmes, unless they are well targeted on hard-to-place groups, run the danger of entailing large dead-weight losses. *Fourth*, there may be cases where work does not pay -- leading to a risk that some benefit recipients may prefer to stay in the programme rather than looking for a job in the private sector. For instance, there are cases where remuneration in public work programmes reportedly competes with market wages in 3-D jobs and, if that is the case, the remuneration of certain programme participants should be reduced as the economy recovers. *Fifth*, training institutions have had difficulties in coping with the rapid and massive expansion of training programmes. For these reasons, there may be a case for increasing resources and staff of training institutions. In addition, the type of training provided by some of them may not be closely tied to the requirements of a complex, modern economy such as Korea. It would be useful to review programme design in close collaboration with social partners.

219. Finally, the role of the PES in programme delivery could be enhanced. The concept of the “one-stop office” is a good one, and should probably be generalised by integrating the separate networks of Employment Security Centers and Manpower Banks. Also, while it may have been useful in the period of rising unemployment to operate another chain of placement offices under the authority of municipalities and other local governments, the co-existence of two types of “public employment services”, one under the Labour Ministry, and one under local government, that are involved in the same types of tasks (apart from benefit payment), may not prove efficient in the long run. As mass unemployment declines, PES officers will need to devote more efforts to counselling and monitoring of disadvantaged groups which run the risk of long-term unemployment and benefit dependency. Needless to say, the efficiency of the PES crucially depends on the quality of its staff and the high turnover of counsellors is problematic in this respect. In present circumstances, improving training and job stability of the staff might be more important than

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increasing the number of officers. The decline in unemployment should provide the necessary breathing space to concentrate on improving the quality of PES staff.

CHAPTER 4 SOCIAL SAFETY-NET POLICIES

A. Introduction

220. A well-functioning social safety-net has become an essential component of modern market economies. The experience of central and east European countries in transition shows that, in the absence of a social safety-net, economic restructuring will be socially unsustainable, in view of workers' resistance to change, thereby endangering the transition process. The recent Asian crisis has also underlined a need for social safety-nets in the countries in question and indeed most of the affected countries have reinforced or, in certain cases, created a social safety-net. At the same time, it is important that the social safety-net, while protecting individuals against labour market contingencies, does not unduly distort the economic incentives to work, invest and innovate. These considerations have motivated the reform of social safety-nets in many OECD countries (OECD 1998*c*; 1998*d*; 1999*b*; and 1999*c*).

221. In the case of Korea, where those in need traditionally rely on support provided by family-members, the social safety-net has been developed later than in other OECD countries. For example, a National Pension System was created in 1988 and, as discussed in the previous chapter, the Employment Insurance System was introduced in 1995. However, because of the newness of these systems, many individuals are not yet eligible for benefit payments. There is, therefore, a need for social assistance support, all the more so because the 1997 crisis led to a marked increase in unemployment and falling real incomes. In the first instance public authorities responded by introducing a set of temporary measures, while at the same time the debate intensified on how a more comprehensive social safety could be developed. In 1999, the Korean authorities enacted a new framework for social assistance, based on its "productive welfare" concept which purports to enhance economic sustainability of the welfare system by reducing administrative inefficiencies, while simultaneously improving adequacy of benefits and maintaining financial incentives in order to avoid the emergence of unemployment and poverty traps.

222. It is not possible to discuss in detail all the pillars of the Korean social safety-net. Instead, the chapter focuses on social assistance policies for individuals of working age. More specifically, the chapter describes the specific context under which these policies operate in Korea. It then examines the extent to which existing social assistance policies cover adequately those in need, while encouraging their reinsertion in the labour market. Finally, the chapter discusses how the concept of "productive welfare" can be made a reality.

B. The changing social policy context

223. Recent trends in poverty and income distribution suggest a need a more comprehensive income support system in Korea:

- Despite the impressive economic performance registered until 1997, a considerable number of Koreans have continued to live in poverty. According to estimates based on the official poverty line, the number of households in poverty declined from 20 per cent in 1975 to about 7 per cent in the mid-1990s (Park

and Kim, 1998). This downward trend came to an abrupt halt with the economic crisis. Available indicators on urban poverty suggest that the poverty incidence peaked in the third quarter of 1998 at around 16 per cent and has abated somewhat since then (PSPD/UNDP, 2000, *forthcoming*, and World Bank, 1999).⁹² In 1999, 8 to 12 per cent of the population had incomes below the official poverty line.⁹³ Apart from job-losers and the elderly, the groups most at risk of poverty include households with low levels of educational attainment, the long-term sick and disabled, as well as large and lone-parent families (Park and Kim, 1998, and PSPD/UNDP, 2000, *forthcoming*). Importantly, about 20 per cent of the Korean middle class now consider themselves to live in poverty while the incomes of other middle class households have moved closer towards the poverty line. Reduced social cohesion is also exemplified by a sharp increase in homelessness during the crisis.⁹⁴

- Income inequality (in terms of both earnings and total income) has also increased, with little signs of improvement despite the ongoing economic recovery (Table 4.1). Over the past three years, average incomes of the poorest 20 per cent of households have declined by over 8 per cent, while average incomes of the 20 per cent richest households have increased somewhat.

224. To address these problems, there exist in Korea four main types of income support systems: *a)* support coming from the extended family; *b)* help from civil society, notably non-governmental organisations (NGOs); *c)* social insurance; and *d)* public assistance. Traditionally, in Korea, the first two pillars have provided an effective social safety-net. However, reflecting changes in Korean society, the role of the extended family has weakened. Therefore, given the limited coverage of social insurance benefit payments, there is a need for a more comprehensive social assistance policy in order to complete the social safety-net.

1. *The weakening of family ties*

225. The role of the extended family as a source of income support is one important aspect of the “Confucian social welfare system”. Its continued importance is underlined by a survey which finds that for a considerable proportion of those in poverty, support from members of the extended family is essential.⁹⁵

92. Different studies on the extent of poverty, while based on the same Family Expenditure and Income Survey, use different estimates on the minimum cost of living as the poverty threshold. These discrepancies are induced by, *inter alia*, different standards for calculating the absolute poverty thresholds (*e.g.* rents). Hence, estimates on the poverty ratio in 1998 vary significantly, ranging from 14 to 25 per cent (PSPD/UNDP, 2000, *forthcoming*).

93. The poverty line is based on the so-called Minimum Cost of Living (MCL), which varies with household size. Importantly, it is used as a benchmark for the calculation of social assistance benefits. In 1999, the MCL for a single-person household was 234 000 won per month, or 350\$PPP. This is comparable to poverty lines of other OECD countries at similar levels of economic development -- *e.g.* in the Czech Republic the poverty line is 320 US\$PPP (OECD, 2000*b*). The MCL is published every year since 1973 and, since 1989, the Korean Institute of Health and Social Affairs Korea (KIHASA) calculates the MCL every five years on the basis of a survey reflecting Rowntree’s basic needs’ approach (Park and Kim, 1998). In between survey years, the MCL is adjusted each year in line with price inflation.

94. The number of homeless persons in Seoul peaked at about 4 700 in February 1999 and decreased to almost 3 600 persons by July 1999. About 90 per cent were in city-run shelter facilities and 40 per cent were in employment -- mainly in public works programmes (*Korea Herald*, 1999*a*).

95. Family support is almost six times larger than public transfers (KIHASA/KLI, 1999). The KIHASA/KLI survey, undertaken in September 1998, reveals that earnings of other household members, relatives and

226. However, the supportive role of the extended family has weakened for several inter-related reasons. First, the proportion of the urban population in the overall population has increased spectacularly, from 17 per cent in 1950 to 77 per cent in 1995. As a result, traditional forms of support, often based on rural values, are being lost. *Second*, the younger generation may be less willing or able to provide support for parents within the household. Traditionally, in Korea, children take care of their parents in old age, which often involves living in the same household.⁹⁶ Between 1984 and 1998, the proportion of old-age people not living with their children more than doubled to 47 per cent (KIPH, 1985, and KIHASA, 1998). *Third*, the distress associated with job loss seems to have increased family break-up and, as a result, the incidence of lone-parent families at risk of poverty is on the rise. In 1998, the number of lone-parent families increased by 10½ per cent to almost 60 000 households (covering almost 167 000 people). Finally, the gradual integration of women in the labour market has also modified attitudes towards family support.

2. *The important role of NGOs*

227. Korea possesses one of the most vibrant networks of “social” NGOs among OECD countries. These NGOs are estimated to run about 1 400 welfare centres (of which about half receive public funding). These welfare centres deal with a wide range of social, medical and re-integration services. They typically provide home-help for the elderly and the disabled and general counselling services. But, depending on their specific focus and financial capacity, welfare centres can also provide shelter for the homeless, medical benefits, rehabilitation services, schooling and training, child-care facilities, and sometimes income support. About 100 of them also function as advocacy groups and they can play a pivotal role in advancing the plight of the most vulnerable in the policy-making process.⁹⁷ A detailed discussion of how these NGOs operate in the field of social assistance and how they interact with public policies is provided below.

3. *The relatively low coverage of the social insurance system*

228. Social insurance programmes are increasingly considered as a system rather than an agglomeration of separate policies. However, despite these efforts, a relatively small share of the population is eligible for social insurance benefits:

- The Employment Insurance System fails to cover a significant number of workers and, as a result, only a fraction of the unemployed receives benefits (see Chapter 3).
- Despite the extension of national pension insurance to the self-employed in urban areas in April 1999, about 54.3 per cent of the employed population over age 18 now pay contributions to the national pension insurance (up from 39 per cent in 1998, NSO, 1999). Full pension insurance benefits will not be paid out until 2008, and hence, most individuals of pension age receive only a small public pension

friends, as well as savings, borrowed funds, and severance payments are the main sources of income support for unemployed persons.

96. This feature is actually supported through tax-deductions for care of dependants and parents.

97. Advocacy groups have their roots in the democratic movement of the 1980s. The then student leaders are often among their ranks. These groups see it as their duty to strengthen democracy in Korea through the enhancement of social justice and the active participation of civil society (*e.g.* PSPD, 1999).

and, in many cases, no public pension at all (Annex B). In addition, the pension system seems to suffer from inadequate funding, raising the issue of financial sustainability.⁹⁸

- To a large extent, the enterprise remains an important provider of social benefits. At present, the most important benefit for job leavers and retirees is the mandatory severance payment. However, most temporary and daily workers do not receive separation allowances. Other legally stipulated employer-provided social benefits are paid maternity leave (two months) and the monthly menstrual leave -- the latter is unique among OECD countries, where relevant provisions are normally covered by sickness benefits. Enterprises can also provide child allowances and other types of benefits which, in other OECD countries would be an integral part of the welfare state. However, coverage of such payments is limited to regular workers only.
- Health care provisions either through the health insurance system or the medical aid programme cover the whole population since 1989. Management of the system is broadly divided in two parts: employees in the private sector are served by 139 private health insurance societies across the country, while the National Health Insurance Corporation with regional offices serves public employees, teachers, the self-employed, and daily and temporary workers.⁹⁹ In 1999, government plans to integrate both systems -- now scheduled for July 2000, incurring the wrath of many private sector employees, who protest against increased contribution levels caused in their view by underreporting of self-employment income which keeps contributions paid by the self-employed artificially low (Korea Herald, 1999b).

229. Reflecting the late development of the social insurance system, government social expenditures are significantly lower than in the other OECD countries, except Mexico and Turkey (Table 4.2).¹⁰⁰ Even when mandatory non-government social programmes are taken into account, Korea tends to spend little on social protection compared with other OECD countries (OECD, 1999d, and 2000c, *forthcoming*). Almost half of total (government and mandatory non-government) social expenditure is devoted to severance payments, other old-age cash benefits and survivor benefits, while 36 per cent is devoted to health (Chart 4.1). By contrast, spending on public assistance, unemployment compensation and ALMPs is small.

98. Pension contributions amount to 9 per cent of the standard monthly earnings and are equally shared among employers and employees. Locally insured workers (*e.g.* the self-employed) pay 3 per cent of (self-reported) income levels, while this contribution rate is planned to increase gradually to 9 per cent in July 2005. Unless pension policies are further modified, the fund will go into deficit by 2022, to be depleted by 2031. Hence, pension reform is under debate, and future measures which involve a combination of benefit cuts, increased contribution rates and retirement ages. For those with a 40 year contributory record, replacement rates have already been cut from 70 to 60 per cent in December 1998, while retirement ages are scheduled to increase gradually from 60 years at present to 65 in 2033. The funds of the public occupational pension programmes for civil servants, the military and teachers are already exhausted, and liabilities are largely financed out of the government account (KOILAF, 1999c, p. 15).

99. Contributions vary from 2 to 8 per cent of the standard wage and are equally shared among employers and employees (whose dependants are also covered). The government subsidises the contributions of the self-employed, so that approximately 39 per cent of all funds for the self-employment scheme are paid by central government. Co-payment rates vary with the type of medical care provided (KOILAF, 1999c).

100. The discrepancy in public social effort between Korea and other OECD countries is slightly smaller than what is suggested in Table 4.2. Unlike Korea where most social benefits, except severance payments, are not taxed, some other OECD countries, *e.g.* the Netherlands, and the Nordic countries, tax benefits rather heavily. Hence in those countries, gross (before-tax) public social expenditure is about five percentage points of GDP higher than net (after-tax) public social spending (Adema, 1999). Average net public social spending in the OECD area is around 20 per cent of GDP.

However, in response to the crisis public spending on ALMPs increased from 0.2 per cent of GDP in 1997 to 2.4 per cent in 1999.

230. Social insurance programmes are largely financed by employer- and employee contributions. The government (also acting as an employer) pays only about 20 per cent of the contributions to pension and health insurance systems; and does not contribute to the accident- or unemployment insurance programmes. In this regard there seems considerable scope for increasing public social effort.

231. Given the limitations of the social insurance system and the weakening of family support, there is a need for a comprehensive system of last-resort benefits that provides adequate support to the approximately 3.6 million Koreans whose earnings fall short of the poverty line.

C. The present social assistance system

232. The provision of social assistance, or last-resort, benefits in Korea is embedded in the Constitution, which states that citizens unable to earn a livelihood due to physical disability, old age or other reasons shall be protected by the state. The most important of the social assistance benefits is the *livelihood protection programme* (LPP) which purports to guarantee a minimum standard of living for the needy. In addition, the government responded to the 1997 crisis by introducing a new programme, namely *temporary livelihood protection* (TLP). In principle, TLP is targeted on unemployed individuals of working age, while LPP has a broader scope.¹⁰¹

233. The number of beneficiaries to both LPP and TLP programmes is close to 2 million in 2000, or about 4.4 per cent of the population (Chart 4.2).¹⁰² Nevertheless, coverage of livelihood protection support is limited to about 55 per cent of the poverty population in 1999 -- the remaining 45 per cent are not covered. The trends in the number of beneficiaries are mirrored in the budgetary allocations of the Ministry of Health and Welfare. As can be seen from Table 4.3, these allocations have doubled since 1997. Even so, these expenditures, at about 5 per cent of the total government budget, remain small.

234. To some extent, the relatively low coverage rates and low levels of spending can be explained by the fact that some would-be beneficiaries do not apply for benefits because either they are not aware of their existence or receiving benefits entails a certain stigma. However, other factors have also played a role, notably the relatively strict eligibility criteria, the low level of benefits and benefit administration problems.

1. The application of strict eligibility criteria

235. Different types of benefits can be provided under the LPP and TLP programmes. These include general income support as well as earmarked benefits for households with children, income support

101. The government also supports a network of social service providers, and through the *medical aid* programme grants free access to health benefits to most of the poor. There is also a small non-contributory pension benefit for elderly persons with low-incomes. Other provisions for low-income households include support programmes for families with children that cover both livelihood protection clients and other low-income lone-parent families (Annex B). Although the Ministry of Health and Welfare (MHW) operates these programmes, they are based on different laws and are administered by different municipal social welfare officers based on specific reporting procedures.

102. Throughout, *beneficiaries* refer to both heads of household and members of the household, *recipients* or *cases* refer to the number of households or heads of households.

towards the cost of living (food, clothing, etc.), maternity aid, funeral grants, and social welfare services, including employment support programmes. Moreover, all livelihood protection clients have free access to medical benefits under the *medical aid* programme. Both livelihood protection programmes distinguish between two broad types of support. *First*, there is *livelihood aid*, in the case of households where no person is able to work due to, *inter alia*, disability, old age (*i.e.* over age 65) and pregnancy. Recipients of livelihood aid are categorised as either clients whose situation necessitates *institutional care*, or clients requiring *home care* support. *Second*, in the other cases, there exists *self-support care*. In theory, recipients of self-support care should have a greater ability to work than livelihood aid ones. However, the actual level of benefits depends on the type of programme (LPP and TLP have different eligibility criteria) and the ability of the recipient to find a job, as perceived by the welfare officer who administers the programme.

236. In 1999, 60 per cent of social assistance recipients were covered by the LPP and the remaining 40 per cent by TLP (Table 4.4). In addition, over two-thirds of all the recipients were entitled to the *self-support care benefit* -- which in theory is granted to individuals who can look for a job. There were proportionately as many recipients of *self-support care* in the LPP as in the TLP. This is somewhat surprising, since TLP is supposed to be targeted on individuals of working age and the expectation was that the proportion of *self-support care* claimants among TLP recipients would have been higher.

237. Benefits under both programmes are subject to means test based on *a*) family income, *b*) individuals' income, and *c*) assets (Table 4.5):

- Family support is traditionally an important plank of the Korean social system, and this feature has led public authorities to include family support conditions in the means test for welfare programmes. In the LPP, the means test is based on the capacity (to earn) of extended-family members.¹⁰³ Among OECD countries, this is an unusually strict interpretation of family support criteria. The usual practice is that actual income is taken into account -- as for example in Switzerland (OECD, 1999c).
- Eligibility for TLP benefits is not based on the earnings' capacity of extended-family members. The benefit unit for the TLP means test is the household defined as persons registered at the same address. Furthermore, asset disregards¹⁰⁴ are about 50 per cent higher than is the case with the LPP.

2. *The low level of benefits*

238. The level of social assistance payments depends on the type of programme, but also on family and income criteria. At maximum, social assistance payments are equivalent to 60 per cent of the official poverty line (Table 4.6).

239. Income support to recipients who are supposed to be unable to work (*i.e.* the recipients of *home-care* and *institutional care* support) is more generous than payments to able-bodied recipients (*self-support care* recipients -- see grey-shaded area in Table 4.6). In addition, income support to *home-care* beneficiaries under the LPP-regime is provided throughout the year and varies with household

103. Thus, under the LPP rules, an elderly couple living in Seoul with a married daughter in, say, Pusan is not entitled to income support, even if actual household income of the daughter in question is barely above subsistence level.

104. The asset test considers cars and even business tools, but mainly focuses on property (houses). Applicants have to declare the balance of their bank account(s), but this information cannot be verified in view of the prevailing privacy laws.

size and earnings of all household members,¹⁰⁵ whereas *self-support care* clients receive benefits during six months only (October to March), and only to the extent that household income is less than 600 000 won (about 900 US\$PPP) (Table 4.6).¹⁰⁶ Benefits provided to able-bodied recipients amount to about one quarter of social assistance payments in Switzerland, and half of what a Czech family in a similar situation would receive (OECD, 1998*d*, and 1999*c*). Finally, it should be stressed that both the *self-support care* and TLP clients receive cash and other elements of livelihood protection support to the extent that earnings do not exceed the set eligibility criteria.¹⁰⁷

240. The level of benefits is related to the official poverty line, *i.e.* the Minimum Cost of Living (MCL).¹⁰⁸ The MCL, and hence benefit payments vary by household size, but not with regional variations in the cost of living, so that the real level of benefits varies across regions. According to a survey by KIHASA, the minimum cost of living for metropolitan areas is 7 per cent above the official MCL, while in the cases of rural areas it is 13 per cent below the official MCL (Park and Kim, 1998).

241. Table 4.6 shows that the elasticity of benefit income for *self-support care* and TLP payments with respect to household size is relatively high compared with what might be termed the international consensus.¹⁰⁹ In particular, equivalence elasticities for the first additional adult are high, but this has to be interpreted in the light of relatively low benefit rates for single people.¹¹⁰

242. Given the low level of benefits, the current public assistance system provides ample financial incentives to work, especially for *self-support* clients and recipients of *temporary livelihood benefits* (Table 4.7). Net replacement rates are among the lowest in the OECD area (OECD, 1999*e* and 2000*d*). Work pays in Korea under the existing rules.

243. *Home-care* support recipients, despite the limited employability of many of them, are encouraged to work through a complex system of earnings' disregards. In other words, recipients who accept a job may keep their benefits to the extent earnings are below a certain threshold. The purpose of this system is to avoid situations where benefit recipients who are employable reject a job offer on the grounds that it is not financially rewarding *vis-à-vis* benefits. Thus, as Chart 4.3 shows, an unemployed recipient who accepts a job paid less than the minimum cost of living can keep part of the benefits, thereby making work pay. However, once the recipient is working, he might not have much incentive to increase his/her earnings, for example by working longer hours. For instance, a recipient who is working and earns 70 000 won, has no

105. Payments to *institutional care* beneficiaries are slightly different from payment rates to *home-care* beneficiaries.

106. About 30 per cent of self-support care clients receive these benefits. The remaining 70 per cent can receive education benefits, medical aid and funeral grants.

107. *Self-support care* clients participating in a public works programme do not receive income support, but remain entitled to education benefits, medical aid, and funeral grants (MHW, 1999*a*).

108. For details on the basket of goods considered in the survey, see Park and Kim (1998).

109. Equivalence elasticities concerning one additional adult in Belgium, Canada, the Netherlands, Norway and Switzerland were 0.33; 0.75; 0.41; 0.50; and 0.53, respectively (OECD, 1998*d* and 1999*c*).

110. There is no international consensus on how much extra income must be given to households in order to preserve the same living standard once an additional member is added to a household. However, OECD (1996) concluded that most estimates fell within a relatively narrow range around a median estimate of the amount given to a single person, multiplied by the square root of household size. In other words, in order to provide the same standard of living as experienced by a single person with an income of 100, a two-person household would need $100 \times 20.5 = 141$; a three-person household 173, etc. Accordingly, the relevant equivalence elasticities are: 0.41 for a two-person household; 0.32 for a three-person household; and 0.27, 0.24 and 0.21 for four-, five- and six-person households, respectively.

interest in earning 10 000 additional won, as a substantial portion of the benefits would be lost, to the point that total income would be lower. In the case of large households, the incentive structure is even more perverse -- this is illustrated by the fact that the curve shown in Chart 4.3 has a downward slope, *i.e.* the higher the earnings, the lower total income (this is due to the very large kinks at 200 000 won -- 240 000 won for four and six person households).

244. The MHW also operates 42 000 places in special public works programmes (on top of the 400 000 places in the general public works programme). As placement in these programmes pays less than the general public works programmes (17 000 won as opposed to 24 000 won -- Kim, D.H., 1999), *self-support care* clients have an obvious preference for participating in a general public works programme. Hence, special public works placements mainly cover the elderly and disabled who would not qualify for the general public works programme.

3. The impact of restricted public budgets on the adequacy of welfare provisions

245. As benefits are not awarded as of right, the public welfare budget can theoretically be restricted to the point that clients may receive less than what they might have been legally entitled to and, in certain cases, they will receive no benefits at all. In order to understand how this can happen, it is important to examine the budgetary process. Each year local governments apply to the MHW for funding for the forthcoming year. Subsequently, the MHW submits a proposal containing a prioritisation among expenditure items to the Ministry of Budget and Planning. This Ministry then decides upon the overall budget while taking the financial status of provincial and district levels of government into account (Chart 4.4).¹¹¹ As the budgetary allocations awarded by the Ministry of Planning and Budget are generally considered short of what is needed to serve all the poor, there is inevitably some rationing in benefit awards. Local governments have to work with a set budget, but do not have the discretion to vary benefit rates for *livelihood aid* and *self-support care*, so as to spread available resources amongst all eligible applicants. Hence, inevitably there is some variation in benefit award across the country: otherwise similar clients may not be categorised in the same manner across the country.¹¹² Moreover, budgetary restrictions limit the number of *self-support clients* who receive cash support. It is also possible that otherwise eligible applicants will not receive any benefits as budgets are already exhausted. Even though supplementary budgets have been made available twice during 1998 and 1999 in view of the crisis, some municipal welfare officers have considered allocated budgets well short of what was needed.

4. The heavy workload of welfare officers

246. Since the crisis, the number of applications for livelihood benefits increased, partly reflecting the introduction of the TLP programme in April 1998. Hence, the administrative burden of welfare officers,

111. In general, about 25 per cent of all tax revenues is raised by local government (OECD, 1999*i*), but central government sets tight rules on local tax rates and other sources of local income, so that variation is extremely limited in this respect. Overall, the financial situation of intermediate levels of government is weak, but subject to considerable variation. In 1998, the richest Metropolitan province -- Seoul, funded 95 per cent of its budget out of local revenue, while in the province of Chonnam local revenue only accounted for 40 per cent of expenditure (NSO, 1999). Through a system of tied grants central government induces some equalisation of resources among local governments: poorer local authorities often get more funds than relatively well-off local governments for the financing of otherwise similar projects.

112. According to the *Korea Herald* (1999*c*), the Board of Audit and Inspection found that MHW-funds were administered inefficiently across regions. For example, the North Kyongsi region with 68 000 unemployed persons received support of 4.3 billion won while Taegu with 88 000 unemployed persons only received 2.6 billion won.

who are in charge of administering these benefits, has increased (Annex B). Across the country there are about 3 000 local government social welfare officers working on 850 000 cases (or 1.9 million persons). That is about 1 social worker per 280 cases, with variation across the country. Caseload-to-staff ratios in Korea are very high compared with most OECD countries. In Belgium and Norway these vary from 60 to 100, while the caseload-to-staff ratios range from 80 to 120 in the Netherlands and Switzerland (in some Canadian provinces the relevant ratios sometimes exceed 150). In view of the relatively administrative nature of the work involved, these high caseload-to-staff ratios observed in Korea may not pose immediate problems. But this may change once the proportion of employable clients increases, and social workers are obliged to take a more active role in re-integration of clients in the labour market.

5. Social services and employment support programmes: the extensive role of NGOs

247. There is a close relationship between the public authorities and NGOs in social policy delivery. Most of the social service facilities are operated by NGOs, and of the about 1 400 NGOs in Korea, about half receive financial support from either the MHW and/or local government. At the local level, welfare officers refer both successful and unsuccessful livelihood protection applicants to the welfare centres run by NGOs. Employment support to low-income families and livelihood protection clients is often organised through welfare centres operated by NGOs. These centres also provide job-search assistance and more direct employment interventions (see Box 4.1).

**Box 4.1 Provision of self-support aid:
the close relationship between public authorities and NGOs**

With the introduction of the “Basic Law for Social Security” in December of 1995, social welfare authorities set a first step towards rationalisation of re-integration measures for livelihood protection clients and other low-income workers (e.g. low-income lone families) with the establishment of self-reliance aid centres. In 1998, there were 17 such centres which provide information to clients about available jobs, job-counselling services, and community-based employment programmes. The self-reliance aid centres are run by local groups but partly or wholly financed by the public budget. Community representatives, civil servants and social welfare officers often staff the management support committee which aims to maintain close relations with local authorities, assign projects to other welfare centres, support the administration of new projects, and advise on “self-reliance” loans to low-income families (Park and Kim, 1998).

Self-reliance loans are available to both livelihood protection clients and low-income, lone-parent families. The credit limit for such loans is 12 million won (about \$10 000) or 25 million won for LPP-clients who can take up a mortgage. Obtaining the loan is conditional to an approved “business plan”. The loan has to be paid back within a ten-year period, with a five-year grace period. The programmes are small and cover about 3 000 livelihood protection clients and approximately about 400 low-income, lone-parent families.

Many NGOs operate so-called “Incubator centres” and the most innovative aspect of these centres is their approach towards initiating community-based employment projects for clients who are often considered to have limited labour market opportunities. A recurrent form of support is for business start-ups by unemployed persons, with gradually declining support from the centre’s professional staff: from intensive day-to-day management in the initial stage; to merely checking the financial accounts at the end of the project. After about three years, firms are to be completely independent. Some of these projects have drawn criticism from local entrepreneurs as establishing unfair competition.

The extensive use of NGOs is advantageous in that their knowledge of community needs allows them to react quickly to emerging demands; it also facilitates experimentation so that best practices can be copied in other regions. However, the effectiveness of such a network depends on the financial capacity of charitable organisations. Inevitably, this means that NGOs without good contacts in either the MHW or local government will not procure much public financial support. This is exacerbated by the regional disparity of centres where the financial capacity of rural governments to support community-based centres is limited. Hence, there is distributional unevenness in service delivery. Moreover, a recent report by the Bureau of Audit and Inspection reveals that exerting control over spending

by NGOs and their accounting procedures is not without difficulties. Some directors of welfare centres seem to have diverted funds to finance private expenditures or centres used funds to finance programmes for which they were not intended (Korea Herald, 1999d).

6. Degree of employability of benefit recipients

248. As mentioned above, two-thirds of the beneficiaries are entitled to self-support care benefits, which are theoretically targeted to able-bodied individuals instead of livelihood aid. However, this should not be taken as evidence that the majority of social assistance recipients are employable:

- the distinction between *livelihood aid* and *self-support care* clients does not fully coincide with the client's ability to work, and Chart 4.5 reveals that almost half the *self-support care* clients under the LPP-regime are either elderly or disabled people. The majority of LPP recipients are of non-working age (see tables to Annex B);
- the level of educational attainment of beneficiaries is low. Only about 18 per cent of them have a high-school diploma or university degree, compared with 58 per cent for the population at large, and 64 per cent have either elementary education or no education at all, compared with 27 per cent on average in Korea (NSO, 1999);
- in 1998, almost 40 per cent of self-support care recipients had a job and an equal proportion were inactive, compared with 14 per cent employed and 60 per cent inactive in the case of livelihood aid recipients (Table 4.8). About one quarter of *home-care* and *self-support care* recipients were unemployed; and
- about half of all clients are estimated to remain on LPP *ad infinitum*. Only one third of home-care clients are estimated to leave the programme for a job (Table 4.9).

D. Introducing the concept of “productive welfare” into social assistance programmes

249. The Korean authorities are aware of the weaknesses of existing social assistance programmes and this has prompted them to enact the National Basic Livelihood Security Law (NBLs) in August 1999. The concept underlying the new social assistance law is that of “Productive Welfare” which is hailed as the new “Korean Welfare Paradigm” (Office of the President, 2000). The purpose is to enhance the economic sustainability of the welfare system. It contains the following elements:

- A basic income support and social protection for the elderly and low-income households.
- A more coherent delivery of existing public policies.
- A stronger partnership with private NGOs.
- Reciprocity in benefit receipt for those who are able to work.
- Promoting clients' employability through ALMPs.

250. The productive welfare concept comes close to recent social welfare reforms in Canada and the United States (OECD, 1999b, and 1999c). In these two countries, “Work for welfare” aims at keeping welfare clients closely attached to the labour market by improving their skills and enhancing the financial

incentives to work. The new Korean social assistance programme will take effect as from 1 October 2000, and at present, the NBLIS should be considered as a “framework” Act, since the exact nature of benefit rules of the new social assistance programme is still under discussion. Nevertheless, the following sections discuss the main elements of the new law and consider how the law can be formulated in a way that takes into account equity and efficiency considerations.

1. Improving adequacy of benefits

251. In view of the avowed policy objectives, it seems desirable to extend coverage of social assistance provisions so as to guarantee support to all those with incomes below the official poverty line. The new system takes some steps in this direction. Indeed, under the NBLIS, income support will be provided to *all* clients (including all *self-support care* clients) throughout the year. Furthermore, the official poverty line, which serves as a basis for the calculation of benefits, has been increased by almost 28 per cent compared to 1999 (for a single person), even though benefits are increased by less than the adjustment made to the poverty line. Nevertheless, despite the good intentions, the NBLIS will not cover the entire population living in poverty and projected social assistance expenditures for 2000 are actually lower than the budget for 1999 (Table 4.3). In 1999, almost 2 million persons were receiving some sort of livelihood protection support, and it is projected that the NBLIS will cover approximately the same number of people in 2001, *i.e.* about two-thirds of the population living in poverty, up from about 55 per cent in 1999.

252. The main reason for the projected stability in the overall number of clients is that eligibility criteria will not change dramatically compared with the current system. In particular, the income capacity, and not actual income, of the extended family will continue to be taken into account when assessing entitlement to NBLIS.¹¹³

2. Enhancing policy coherence

253. In contrast to current assistance programmes, the NBLIS is to award benefits as of right which underlines the need for careful monitoring of programmes as well as overall policy coherence.¹¹⁴ In all rights-based cash-support systems moral hazard can become a significant problem (OECD, 1998c; 1998d; and 1999c). In the case of social assistance, most recipients are required to fulfil certain conditions in order to be eligible for benefits and local administrators must determine whether clients actually satisfy these conditions. But these administrators may not have an incentive to apply the rules strictly, particularly when decisions are marginal and difficult and when they do not perceive any clear budget constraints. Additionally, time spent checking whether applicants satisfy conditions for benefit receipt may reduce the resources available to other activities. Therefore, introducing a fully-fledged cost-sharing mechanism might induce a rapid increase in caseloads.¹¹⁵ For this reason it seems preferable to maintain the current

113. Compared to existing benefit rules, eligibility criteria under the NBLIS will change in that the separate asset and income criteria are projected to change into one income threshold (including an imputed income stream from existing assets). But the effect of this change on overall client coverage is likely to be small.

114. As from October 2000 social assistance clients will be able to appeal against award decisions. In the first instance, the local livelihood security commission will deal with appeals, but ultimately clients could seek recourse in the courts with unknown budgetary implications. It is reasonable to assume that the move towards a more transparent set of entitlement criteria will increase the number of successful claims

115. A fully-fledged cost-sharing mechanism gives local authorities the certainty that for every 20 won they spend on social assistance, they receive 80 won from central government. This may induce caseloads to

budgetary “tied-grant” based system for the time being, and not give the certainty to local governments that their financial demands will always be satisfied. To cover for unforeseen circumstances, the creation of a reserve fund could be considered. The reserve fund may also be used to cover local shocks, such as the closedown of a particular industry on which one area is heavily reliant, and which may induce a rapid increase of claims (see Box 4.2).

Box 4.2 Coherent implementation of welfare policies

In Korea, as in most OECD countries, one of the main reasons for using local governments is the belief that this induces a better reflection of local preferences and conditions in social assistance policy. Furthermore, local governments are best placed to apply knowledge about clients and thus decide who of the potential clients in their area might be in the greatest need, to pursue fraudulent behaviour and assess individuals’ labour market prospects (OECD, 1998c; 1998d; and 1999c). However, for the gains of local government involvement to materialise, a coherent policy structure is needed.

In the current system, there would seem to be three important impediments to policy coherence. *First*, social assistance benefits are mainly funded by central government, while their administration is carried out by local government. Indeed, central government bears about 80 per cent (subject to variation across the country), and the remainder is shared among district and provincial governments (who have no other obvious role in social assistance policy). As a result, district governments may have little financial incentive to control eligibility criteria, pursue fraud or effective re-integration strategies for welfare recipients. Possible financial savings for local government of better control in one year may lead to lower central government transfers the following year, so that local governments may actually have an incentive not to reduce caseloads. *Second*, central government financial transfers do not take sufficiently into account the social-economic situation of different municipalities. This may lead to unevenness in benefits across the country (Section C.3). *Third*, local governments may be induced to pursue policies which might be contrary to overall social policy objectives. In the Korean case, the scope for district government, to off-load clients to other social programmes is limited. Nevertheless, if district governments manage to place clients in public works programmes, these persons re-qualify for unemployment insurance if they complete two consecutive work placements of three months’ duration. If public works programmes are fully financed by central government, the incentives to district government to off-load clients are obvious. Although the financial gains accruing to district government from rent-seeking behaviour are currently small, these are likely to increase with the expansion of the NBLs.

In the face of similar problems, certain countries such as Canada (OECD, 1999c) have introduced a so-called “block-fund system”, whose size varies with local socio-economic conditions. This system gives local governments more discretion in dealing with clients as well as sufficient financial resources to do so. In such a setting, local governments have relatively wide responsibilities for implementing social assistance policy; they can also adjust policies to local needs, while having strong financial incentives to pursue entry-conditions, police fraud and help clients off welfare rolls. In Korea, a country with a centralised administrative tradition, it may be too early to envisage the introduction of a “block-fund system”. However, under the new productive welfare paradigm, the gains to be made out of a more coherent policy implementation will increase. Hence, it seems appropriate to gradually decentralise some of the responsibilities in the area of social assistance policy, together with the corresponding financial resources.

3. Introducing work testing of clients and fostering their employability

254. Making productive welfare a reality requires administrative officers to screen clients on their work ability and provide effective employment-oriented counselling services. In turn, this requires a shift in administrative culture, additional resources and co-operation between social assistance and employment agencies. The concept of productive welfare simultaneously introduces reciprocity in benefit receipt and thus the policing of job-search activities and the possibility to provide mandatory training and work

increase rapidly over the years, as local governments have weak financial incentives to administer tight entrance criteria, pursue fraud, or help clients of welfare rolls into work.

placements for those who are able to work. Based on the experience of other OECD countries with the re-integration of social assistance clients, it is possible to trace out several policy avenues towards an effective pursuit of re-integration strategies of social assistance clients.

255. *First*, the NBLIS should assign a high priority to the establishment of individual plans on the basis of client characteristics. Such an approach requires intensive involvement of the case manager. At present, however, there are about 250 clients to each welfare officer, so that staff simply do not have the time to screen and adjudicate clients on their work-ability or provide intensive job-counselling services. The authorities have undertaken to hire additional social workers (and to provide relevant training) so that caseload-to-staff ratios decline to about 1 per 200 households (4 200 officers working on about 850 000 cases). But this would be still well above the OECD norm of about one officer to 80 to 120 clients.

256. *Second*, identifying client needs is most effective when case-managers have adequate funds to procure the delivery of training, work placements or intensive job-counselling services. If the NBLIS were to serve all the unemployed, except those served by the EIS, this would suggest integrating the delivery of all employment support services in the NBLIS framework, whilst making case-managers responsible and providing them with the necessary funds to perform re-integration strategies and avoid unnecessary duplication. Re-allocation of budgetary resources and administrative responsibilities would therefore be required. For example, a certain share of the general training budget could be re-allocated to the NBLIS authorities, who could then “buy” training services on behalf of their clients. This would also provide case-managers with the leverage to exert influence on the design of training programmes and to make them more relevant to the learning abilities of their clients and the needs of local employers. Likewise, it can be argued that certain public works programmes could be integrated in the NBLIS framework (Park, 2000). In the current set-up employment security centres are financed out of the employment insurance fund, and therefore, have no financial incentives to place NBLIS clients. As in other OECD countries (OECD, 1998, 1998a and 1999), the PES tends to focus on the placement of unemployment benefit recipients who are relatively well-qualified, whereas social assistance claimants are likely to be predominantly those who are the most difficult to place.¹¹⁶ In order to enhance the quality of employment services and improve the financial incentive structure, the Dutch public employment service was recently reformed, so that municipalities responsible for the re-integration of social assistance clients can now “buy” employment support services as training and work placements from both public and private providers (OECD, 1998d, NYFER, 1999).¹¹⁷

257. Therefore, complementarities with private employment agencies could be enhanced (Chapter 3). Private agencies are very experienced in placing low-skilled workers. In Korea, however, the authorities seem reluctant to use them, which seems rooted in the bad reputation of private agencies.¹¹⁸ Nevertheless,

116. Delivery of employment services to current social assistance clients is limited. There is little co-operation between staff of employment security centres and manpower banks with municipal welfare officers. Sometimes, welfare officers have never even visited these centres, let alone established a working relationship with relevant staff. The relationship between welfare officers and job-information centres run by local government is much tighter, as welfare officers know their colleagues at local government level, while local governments also have financial incentives to help welfare clients making use of their centre.

117. In the mid-1990s, the Dutch PES budget was split in two parts: a “basic budget” (for job-brokerage) and an “output budget” earmarked for the re-integration of benefit recipients (OECD, 1998d). During the second part of the 1990s this output budget was re-allocated from the PES to public institutions responsible for the operation of social insurance and the municipalities who are responsible for social assistance delivery in the Netherlands. Until 1 January 2000 these municipalities and social insurance bodies were obliged to “buy” re-integration services with the PES, but since the beginning of this year municipalities and social insurance bodies are entirely free in choosing the provider of re-integration services for their clients.

118. Private agencies are often deemed to provide bad jobs while their coverage in rural areas is low. According to anecdotal evidence, some of them are alleged to be corrupt and involved in prostitution.

private agencies have a considerable market share (Chapter 3), and the authorities could consider the implementation of some pilot projects, allowing private agencies to tender for the provision of employment services to NBLs clients. The fee to agencies for handling these clients, to be paid out of the NBLs budget, could be made partly or wholly dependent on their success of providing jobs to clients, these jobs could be subject to a minimum duration in order to reduce the risk of fraud. If these pilot projects prove to be successful, the scope of complementarity between public and private employment services for the placement of social assistance clients could beneficially be expanded.

258. *Third*, as well as being tools in the worktesting strategy, ALMPs can also enhance participants' skills and employability. Except for a relatively small group of readily employable NBLs clients, the characteristics of current welfare recipients suggest that ALMPs often have to serve older and disabled workers with low levels of educational attainment. To use limited available resources most effectively, careful consideration should be given to the design of programmes and the selection of its participants.

4. Enhancing financial incentives to work

259. All rights-based cash-support systems lead to "benefit traps" as clients (and their families) may prefer to rely on assistance rather than seeking to improve their position through work or taking steps to improve their employability. This risk is limited in the current assistance programme: *self-support care* clients only receive cash support at low rates for at most six months, if at all, and replacement rates are therefore low. In addition, social pressures to work in Korea are strong. But the new social assistance law may entail a greater risk of benefit traps. With benefits awarded as of right and income support to employable clients extended throughout the year, there is a theoretical possibility that reliance on benefit as the main source of household income will increase if benefit payments increase substantially from current levels.

260. As long as payments to employable clients do not even match the poverty line, it is to be expected that families will have to rely on casual, part-time or temporary earnings to raise their incomes. Strictly speaking, such work is not compatible with continued receipt of benefit, but the scope for fraud seems considerable, in particular in view of the opportunities to combine benefit receipt and daily work in the large informal sector. There are strong arguments in favour of structuring the NBLs so as to permit households in difficult circumstances to improve their situation by combining benefit receipt and work. Such work may provide a route back into the regular labour market (OECD, 1997d). To achieve this, a system of "earnings disregards" is required. However, such a system should be rather different than the current earnings disregards for *home-care* clients (Chart 4.3). In thinking about earnings disregards, it is necessary to find the appropriate balance between *a*) providing incentives to engage in part-time work; and *b*) becoming fully self-reliant. If the rate of withdrawal of benefit is too rapid, the incentive to work part-time is restricted; if it is too slow, the option of combining part-time work with benefit receipt becomes too attractive relative to working full-time and exiting the benefit system altogether. There is no international consensus on what the appropriate claw-back rates for different earnings ranges should be, or on the level of earnings from where the claw-back rates should apply. However, as payments to *self-support care* clients are well below the minimum subsistence level, adequacy considerations seem to imply that clients should at least be allowed to keep all their earnings below the poverty line. Above the poverty line, the earnings disregards could be gradually phased out. This would mean that clients have sufficient incentives to earn at least at subsistence level, whilst ensuring that full-time work is still far more attractive than benefit receipt.

261. To enhance the financial incentives to work, the authorities could also reconsider the contributions to medical insurance. Livelihood protection clients are covered by medical aid for which they pay no contribution. A casual or daily worker with low earnings has to pay his contributions to the

National Health Insurance Corporation. The fact that being in work implies losing free medical coverage has been found to be a significant barrier to work for low-income families in many OECD countries (OECD, 1998*d* and 1999*c*). Possibilities of reducing the disincentive to work include reducing the contribution rate of such families to the health insurance programme, or otherwise ensuring the provision of health care at a low cost for low-income families (as for example in Canada).

262. The absence of child-care facilities also can deter married woman, or lone-parents from labour market participation. At present, child-care facilities are not fully adequate, but the Korean authorities are rapidly increasing capacity (Annex B). This benefit may thus help low-income lone-parent families to be in employment. However, as this benefit is to be provided to all families with children on social assistance, and not all low-income families with children, it simultaneously acts as a deterrent to work for couples with children as they lose free child-care services once they move off social assistance. Therefore, priority can be given to making this benefit available to all low-income families.

5. Final policy considerations

263. Korean social policy is undergoing profound changes. Having initially reacted to the crisis with the rapid introduction of temporary measures, the Korean government is now in the process of adopting a comprehensive rights-based social assistance system. The challenges it is facing in this process are considerable.

264. *First*, social assistance will have to cover all those in need and the level of benefits would have to be raised to the minimum level of subsistence. This policy aim might not be immediately achievable in view of the financial implications, but it should remain a key medium-term policy goal. It might imply that social expenditure grows more rapidly than other government outlays, but the relatively low level of social spending in Korea suggests there is scope to fund such an expansion.

265. *Second*, as experience in OECD countries shows, the creation of a comprehensive social safety-net can be very costly in the presence of programme inefficiencies and when financial incentives for a cost-effective administration of the system are weak. Efficiency gains can be made by the integration of existing welfare policies and administrative procedures. The elimination of the temporary livelihood programmes while covering most of its clients in the NBLIS is a first step. It could also be considered to integrate the benefits that are provided under the Infant Care Act in the NBLIS. Strictly separating programmes for low-income households seems wasteful, especially if different welfare officers with different reporting procedures manage these programmes. The case for involving local government in assistance provision can clearly be made, but the involvement of provincial government seems difficult to rationalise.

266. *Third*, it may be wise to re-allocate budgets and responsibilities, so that case-managers can effectively procure the delivery of training, work placements or intensive job-counselling services for their clients. This would also provide case-managers with sufficient leverage to modify the programmes to their clients' needs where necessary, while it would strengthen the financial incentive structure for providers of employment supports.

267. *Fourth*, the implementation of an effective labour market re-integration strategy that includes work testing will require a significant change in administrative culture. Dealing with employable clients requires a different attitude than the present more administrative role of public welfare officers. More time will be needed to scrutinise applications, pursue fraud, and most importantly get clients off welfare rolls through intensive job counselling. Current caseload-to-staff ratios are high and it seems that further

investment in hiring and training quality social workers will be needed to strengthen the labour market re-integration function.

268. Finally, the drive to improve adequacy of social assistance benefits should be balanced with labour market considerations. The conjunction of income support payments, earnings disregards and medical and educational support benefits should be so designed that the new comprehensive social safety-net system will continue to guarantee strong financial incentives to work for clients, so that work continues to pay in Korea.

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