

Wage Structure Reform and Labor Market Flexibility: The Case of South Korea

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I. Background to the Discussion on “Reforming the Wage Structure”

The Act on Age Discrimination Prohibition in Employment and Promotion of Employment of the Elderly (“Elderly Employment Act”) as amended on April 30, 2013, raised the minimum retirement age to 60 years and requires the undertaking of measures to accommodate this retirement extension such as amending the wage structure. According to Statistics Korea, Korea is projected to be an aged society by 2017 (with 14.3% of the total population over the age of 65) and a super-aged society by 2026 (20.8%).

Table 1. *Highlights of the Amended Elderly Employment Act*

- (1) Employees’ retirement age shall be at least 60.
 - Applicable to workplaces and public organizations with 300 or more employees: effective January 1, 2016.
 - Applicable to workplaces and central/regional autonomous bodies with fewer than 300 employees: effective January 1, 2017.
- (2) Requirement to undertake measures necessary to accommodate retirement extension, such as amending the wage structure, depending on the workplace’s circumstances.

In an era of population aging and low growth, or jobless growth, the retirement-age guarantee and job security must be backed up by reasonable income distribution. Given the limited ability of the current education/seniority-based framework to ensure such a distribution, it is necessary to overcome this framework, starting with revising the wage or job structure.

The wage structure is a framework of standards that determine the base wage, one of many wage types that also include allowances and incentives. But the definition of the standard differs from person to person, and thus the names are many and numerous. This is

because the base wage is determined by contracts between labor and management and thus cannot be imposed by institutional mechanisms such as laws.

The standards for determining base wages are largely based on three elements: people, work, and competency. In other words, the base wage can be determined by a person’s external circumstances such as education, age, or years in service; the importance of his or her work, or how valuable or indispensable it is; and how competent he or she is in performing it.

Based on these standards, the terms used are seniority-based pay (based on the “people” element), job-based pay (based on “work”), and competency-based pay. Where skill is given priority over qualifications or competency for determining the base wage, it is more reasonable to call it skill-based pay than competency-based pay.

The current pay structure in Korea—or the base-pay determining mechanism, more specifically—is summarized in Table 2(as found through the Workplace Labor Survey conducted in June 2012). Because how base pay is administered depends on the main criteria that determine the base-pay amount, the survey asked respondents to list all types of base pay that apply to their workplace.

Table 3 shows that step pay has the highest distribution, followed by competency-based and job-based pay. In addition, the table shows that workplaces rarely use a single wage structure, instead mixing several components, and that step pay is given the greatest weight in most cases. Only 4.2% responded that their pay structure is purely job-based. This shows that although there is broad consensus on the need to modify the pay structure, such an effort could encounter challenges in the real world if the right process and order are not found.

Table 2. *Types of Pay Structure Determining Base Pay*

Base Pay Determining Mechanism	Description
Step pay	Wage determined based on years in service (step pay or years-in-service pay).
Competency-based pay	Wage determined by evaluating the extent to which a worker possesses the qualifications deemed essential to performing a job (competency-based pay or qualifications-based pay).
Job-based pay	Wage determined by type of job, based on evaluation of the job itself.
Other	Wage determined by a scheme other than step pay, competency-based pay, or job-based pay.

Note. From *Workplace Labor Survey*, by Ministry of Employment and Labor, June 2012.

Table 3. *Distribution of Base-Wage Types in Workplaces with 100+ Employees (N= 10,374)*

Type	Step pay	Competency-based pay	Job-based pay	Others	Share (%)
1	X	X	X	X	0.0
2	O	X	X	X	21.5
3	X	O	X	X	4.7
4	X	X	O	X	4.2
5	X	X	X	O	8.8
6	O	O	X	X	10.7
7	O	X	O	X	5.9
8	O	X	X	O	6.1
9	X	O	O	X	2.8
10	X	O	X	O	1.3
11	X	X	O	O	1.8
12	O	O	O	X	5.7
13	O	O	X	O	0.5
14	O	X	O	O	0.4
15	X	O	O	O	0.9
16	O	O	O	O	24.7
Total	75.5%	51.4%	46.5%	44.6%	10,374

Note. “X” indicates that this type of base pay does not exist, and “O” means that this type of base pay does exist.

For the short term, it is necessary to establish the framework for a guaranteed retirement age and job stability, preferably before the new retirement-age law (mandating age 60) goes into effect. In addition, it is necessary to add job, competency, and performance criteria to the framework of seniority-based pay, and to ensure that the job structure is linked to job, competency, and performance criteria by ensuring job rotation and diversifying career paths. It is also necessary to use the wage peak system to counter restructuring by the business targeted at elderly workers to ease the cost burden, while developing jobs that are better suited to elderly workers whose wages have declined.

For the medium to long term, it is necessary to ensure that the framework of retirement-age guarantee and job security is solid, which will take some time. If realized, this would move the bases of the wage and job structures from education/seniority to job/competency/performance. The overall HR management system, such as mechanisms for hiring and evaluation, should also transition to a more job/competency/performance basis, and there should be efforts to build social consensus regarding wage levels and wage gaps.

II. Wage Structure reform: policy experience

1. Overview of past experience

It should be noted that this is not the first case of the government's policy thrust to improve the wage system. It is important to learn from the past experience to identify the limitations and reflect the lessons in future policy-making. Efforts to improve the wage structure in Korea began to be shaped around 20 years ago. As its economy became more open and market-oriented, businesses began to lose competitiveness and jobless growth patterns began to emerge, prompting calls for a more flexible wage system that can replace the rigid and collective seniority-based wage structure.

One good example is the wage peak system that was introduced since the 1997 Asian financial crisis which quickly became the biggest crisis in the history of the Korean economy. "Wage peak system" then was an unfamiliar term, which involved freezing or gradually reducing the wage level over a few years leading up to retirement, with the aim of lessening the burden on businesses while easing the pressure on employees to retire earlier. It continues to spread slowly across the Korean economy to this day. On one hand, businesses strongly prefer this system as a way to reduce labor cost in time for the longer working life, while unions stand against it. For its part, the government has been trying hard to introduce the wage peak system in the public sector: in fact, the adoption rate today is higher in public institutions.

Aside from the wage peak system, the annual salary system was also introduced as a policy instrument to improve the wage system. It is a scheme that places emphasis all total compensation, not monthly pay, and has caught on fairly broadly. But although it continues to spread among businesses, the seniority-based wage structure has not gone away. Rather it has combined with the annual salary system, spawning a so-called Korea-type annual salary system that is now the main form in many Korean companies

As many criticized that the annual salary system was in name only (that in fact wage was still determined by the wage step), some are also trying to adopt the job-based pay scheme

outright. But it is still rarely used among Korean companies, with most lacking even the rudimentary preparation to adopt the system.

In the end, there have been numerous efforts and cases of improving the wage structure but mostly without the fundamental effort to change the basic pillar of wage management from individual-based to job-based. As a consequence, none of the initiatives so far, be it wage peak system, annual salary system, job-based pay or open contract employment, broke away from the nostalgia for or inertia from the high-growth era when it was believed that pay raise should be determined by years of service. As a result, there is an enormous wage gap today between oligopolistic large companies/public corporations and SMEs and between regular workers and non-regular workers. And in a principal-contractor relationship, the wage ratio between the workers of the two companies performing similar jobs is on average 50% or even less, leading to escalating conflict.

The followings will take a deep look into the evolution of wage scheme in Korea with focus on the wage peak system, annual salary system, and job-based pay scheme, identifying the characteristics and limitations of each.

2. Wage peak system

Wage peak system is designed to ensure continuous employment for workers. It involves adjusting the wage level over a certain period of time in exchange for employment guarantee (by extending the retirement age or post-retirement employment) after a certain age as determined by labor-management agreement. It is a scheme expected to bring about stronger employee motivation and efficiency, to be achieved by reducing labor cost, heightening productivity while easing anxiety of early retirement among older workers. The wage peak system appeared as a complement to seniority-based scheme, a transitory wage system that appeared in the course of moving to job-based and performance-based wage scheme. It has been offered as an option to address the issue of population aging by encouraging hiring of older workers.

As the workforce continues to age, Korean companies are attempting to restructure their workforce and switch over to a performance-based compensation system such as the annual salary system to reduce labor cost burden that arises from the current dominant form of wage

system, seniority-based pay (step pay). As part of such reform, the wage peak system has been positively received (Hwae-Seong Lee, 2005).

The government is also actively communicating its usefulness as a way to address population aging and shortage of youth and middle-age labor. Incidentally, a system that is similar to the wage peak was adopted by some financial institutions in Korea starting in 2001, and part of it remains in operation.

The formal wage peak system was first adopted by Korea Credit Guarantee Fund in July 2003. <Table 4> is a summary of the reasons for and benefits of adopting the wage peak system. Today it actually exists in a number of different types, as shown in <Table 5>, but the most common type is the “retirement age guarantee system” where the employee's wage is downward adjusted starting from a certain age in exchange for guaranteed employment until the retirement age.

Table 4. *Wage Peak System: Reasons and Benefits*

Reasons for adoption	Benefits
<ul style="list-style-type: none"> - Main instrument of restructuring after financial crisis - Rapid population aging in society and businesses - Rising labor cost from seniority-based pay - Domestic/global economic volatility and slowdown 	<ul style="list-style-type: none"> - Stronger job security for older workers - Retention of skilled workers - Ability to hire new workers - Fewer labor-management conflicts over dismissals - Higher lifetime income for workers - Stronger post-retirement security - Less burden on social security, stronger/undiminished growth potential for the national economy

Table 5. *Types of Wage Peak System*

	Retirement age guarantee	Retirement age extension	Employment extension
Objective	Labor cost reduction	Employment security	Employment security
Motivation	Medium	High	High
Employment type	Regular (reallocated) / Special employment	Special employment / Fixed-term contract	Fixed-term contract
Extension period	Short	Medium	Long
Job specialization	-	High	High
Remarks	Retirement age unchanged	Retirement age extended	Employment extension is determined at the time of reaching retirement age

According to the *Supplementary Survey on Labor Force Survey at Establishments* conducted by the Ministry of Employment and Labor (MOEL), the rate of adoption of the wage peak system at all workplaces with 100 or more employees was on a path of moderate growth: 9.2% in 2009, 12.1% in 2010, 12.3% in 2011, and 16.3% in 2012.

The survey indicates that while the wage peak system is on a growth trend ten years after its introduction, not many companies are putting it to actual use. This is mostly attributable to labor's opposition to wage reduction and the difficulty in developing or switching to jobs suitable to elderly workers. But the system is gaining renewed interest from businesses in the wake of the legal revision extending the retirement age to 60.

It appears that there are sharp differences between labor and management over the wage peak system. Businesses take it to be an inevitable and important option that can help lessen their burden of longer employment, but labor remains wary of its spread as it would lead to wage reduction. It also fears that longer employment will only lead to increase in fixed-term contract employment.

Some also point out that the wage peak system is mostly suitable for large companies. SMEs are rarely in the position to adopt the system because most of them offer low wage or do not have employment guarantee until retirement age. At the same time, union's opposition is a tough challenge for them to overcome when trying to adopt a system that involves wage

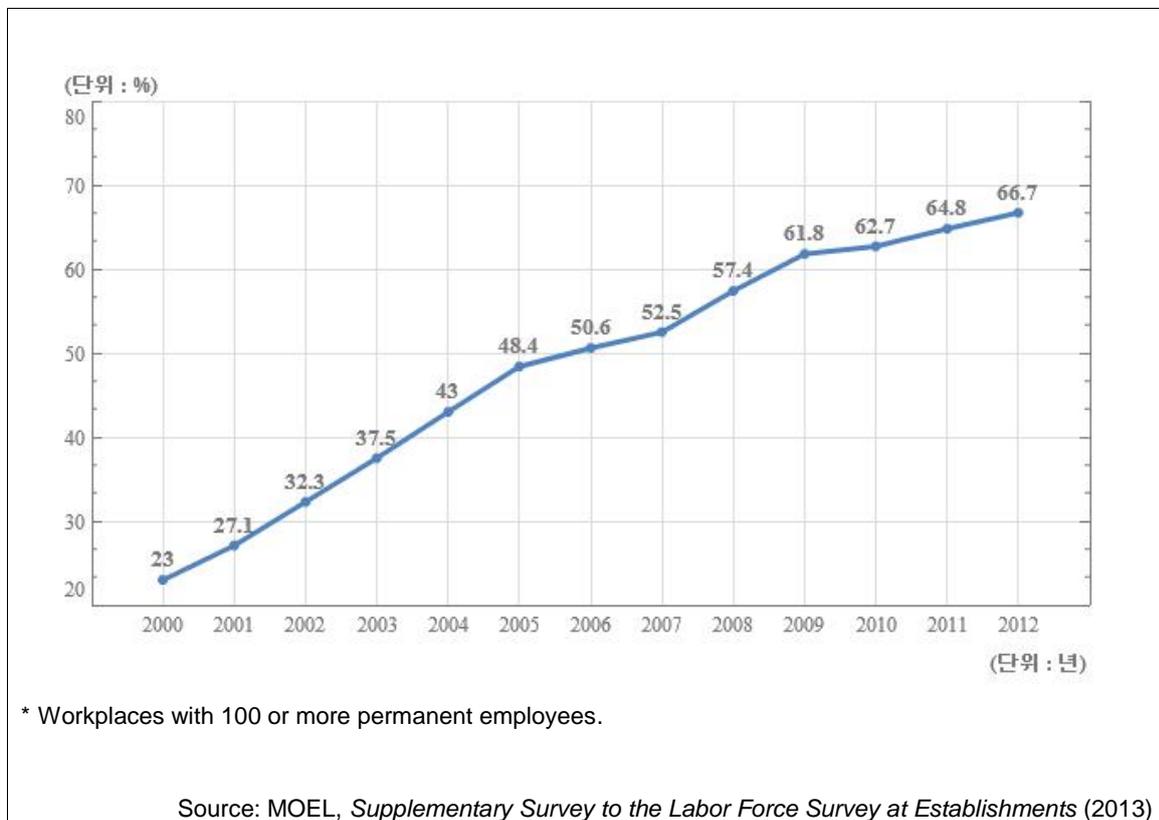
reduction. But consent from workers' representative is a requirement for adopting the system.

3. Korea-type annual salary system

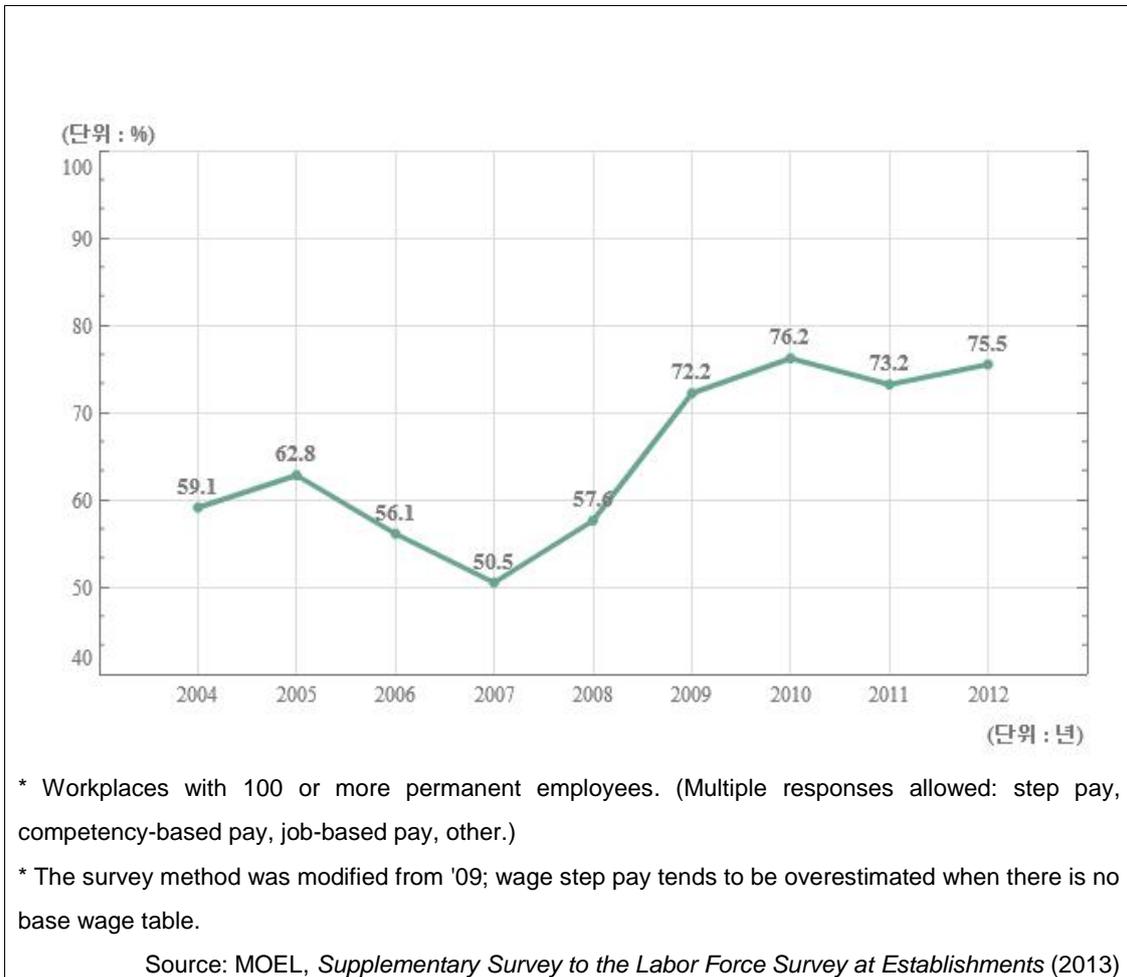
The annual salary system was introduced after the 1997 Asian financial crisis as Korean companies tried to change their HR management to better suit market competition. While the adoption rate was only 1.6% in 1996, it jumped to 23.0% in 2000 and 52.5% in 2007. But some observe it has reached a saturation point. The pace of increase has been slowing down recently, while only a few businesses responded that they are in preparation or are planning for it (Dong-Wook Um, 2009).

Despite the current adoption rate of 60%, as seen in <Figure 1>, there are signs that perhaps the salary system is not being administered according to its principles. For one thing, the step pay system, which was targeted for replacement by the annual salary system, has remained stubbornly unchanged as seen in <Figure 2>.

<Figure 1> Annual Salary System at Korean Companies



<Figure 2> Step Pay System at Korean Companies



According to the *2012 Pilot Survey on Wage Information* undertaken by the MOEL, among 617 Korean workplaces, a higher number was found to have the annual salary system (57.1%) than the wage step (50.3%). But comparison of wage increase rate at 20th year of service among workers with at least a university degree shows that the annual salary system actually has a stronger element of seniority-based pay: annual salary rose by twofold from the initial wage, higher than the 1.9-fold increase under the wage step system (Maile Labor News, 2013).

In the public sector, it began with the annual salary system for government employees adopted in August 1998 as part of the public sector reform. Given that the government had an important role, dissemination of the annual salary system in Korea can also be seen as the consequence of institutional isomorphism pressure (Dong-Bae Kim & Jin-Ho Jeong, 2006). The annual salary system was accepted as the means to replace the existing rigid form of

seniority-based wage system, to be a form of (Korea-specific) performance-based wage system ensuring differentiated compensation depending on individual performance evaluation (Gyu-Chang Yoo & Woo-Seong Park, 1999). It appears that there was a strong motivation to reflect the differences in performance but not enough thinking on compensation differentiation by job..

In short, the annual salary system found in Korean companies is a limited or partial version of the one in the west, with a diverse and even vague typology. But it does appear to be more similar to the system widely used in Japan rather than that of the US, which is closer to a pure salary system. <Table 6> below provides an overview of the Korea-specific salary system.

Table 6. *Features of Korea-specific Salary System*

Issue	Description
Performance evaluation	<ul style="list-style-type: none"> - Low awareness in the beginning on the importance of performance indicators - Using generic indicators rather than developing company-specific ones.
Low motivational effect	<ul style="list-style-type: none"> - The feedback loop allowing competency/performance to be reflected in salary, “job → evaluation → salary” is incomplete
Inflexibility of the wage system	<ul style="list-style-type: none"> - Separate contracts for wage and employment, making it impossible to terminate employment contract citing expiration of the salary contract (annual salary is based on one-year wage contract)
Statutory severance pay	<ul style="list-style-type: none"> - Not part of the “pure” annual salary system in major economies - In light of the spirit of Article 34, Labor Standard Act, it is not appropriate to include severance pay in the monthly payment of the annual salary.
Ordinary wage vs. average wage	<ul style="list-style-type: none"> - Average wage is becoming the ordinary wage because of the annual salary system - Items that were included only when calculating the average wage are now all included in the annual salary which is then prorated by month, causing “ordinary wage” to rise.

Various issues arise from the aforementioned characteristics of Korea-specific salary system. Some of them will be reviewed in this section through case studies. GM Korea (then GM Daewoo) switched to performance-based salary between 2000 and 2002 for executive level employees under which salary compensation will be differentiated by personnel

evaluation. It was then spread to all employees from 2005. And from 2006, it became the first automaker to apply individual salary system to office workers, sparking confrontations with the union.

At the time of introducing the salary system, there was little job security at the company as it undertook layoffs. And after the system was implemented, the wage level was determined without a negotiation process, based only on the team leader's evaluation score. This led to wage differences, and combined with the restructuring ongoing at the time, it further stoked employees' discontent. The office workers' union demanded the salary system to be abolished and seniority-based pay to be adopted starting from 2012.

Finally in 2013, labor and management agreed to abolish the salary system for office workers and to develop a new wage scheme based on seniority. GM Korea is cited as a case illustrating the ill effects and limitations of an annual salary system adopted without an objective set of performance indicators (Maeil Labor News, 2013).

4. Job-based pay system

Although experiments with wage peak and annual salary system are still ongoing, the need to develop job-based pay is once again gaining urgency among Korean companies. This is because job-based HR management is important to ensure employment security and labor cost reduction at the same time as retirement gets pushed back.

At the same time, a new employment type emerged called "open-ended contract employment" in the wake of legal enactment calling for reduction of non-regular workers and conversion of long-serving fixed-term contract workers to regular employees. It is a compromise between non-regular and regular types: the wage level is kept lower than that of regular workers (by not applying the wage step or reducing the initial salary) but employment is guaranteed until the retirement age.

This also renewed the necessity to adopt job-based pay to establish the basis that their jobs are different from those of regular workers and to facilitate long-term wage management. The wage structure for open-ended contract workers has become a contentious issue in the public sector. The management sometimes allows the wage step to be applied to open-ended

contract positions at the demand of the union and the workers themselves because of the difficulties in designing a job-based pay scheme.

According to the *Status Survey on Labor Rights of Open-ended contract Workers* conducted by the National Human Rights Commission in 2008 (<Table 7>), 25.9% of open-ended contract workers responded that step pay was newly applied after being converted to open-ended contract status, 8.2% was applied with job-based pay, and 6.1% performance-based pay. Notably among women open-ended contract workers, it was found that wage step was applied less frequently than men (71.2% and 38.8% respectively).

Table 7. Change in Wage Scheme Before and After Conversion to Open-ended contract Status (applicability of the wage step)

(Unit: 1 person, %)

			After conversion		
			Applied	Not applied	Total
Before conversion	Step pay	Applied	186	24	210
			29.2	3.8	33
		Not applied	165	262	427
			25.9	41.1	67
		Total	351	286	637
			55.1	44.9	100
	Job-based pay	Applied	91	7	98
			15.2	1.2	16.3
		Not applied	49	453	502
			8.2	75.5	83.7
		Total	140	460	600
			23.3	76.7	100
Performance-based pay	Applied	161	15	176	
		27.1	2.5	29.6	
	Not applied	36	382	418	
		6.1	64.3	70.4	
	Total	197	397	594	
		33.2	66.8	100	

Source: National Human Rights Commission, *Status Survey on Labor Rights of Open-ended contract Workers* (2008)

According to the survey on *Policy Direction on Non-Regular Employment in the Public Sector* conducted by the Korea Labor Institute in 2013, 36% were found to apply step pay to open-ended contract workers (Juyeop Ahn, 2013). Through its “Measure on Non-Regular

Workers in the Public Sector,” the government is focusing on improving job security and treatment of non-regular workers with focus on conversion to regular employment or open-ended contract status. But what labor is demanding as better treatment is application of the wage step, and the government has yet to present any meaningful guideline on introducing job-based pay that can counter the demand.

It should be noted that job-based pay was introduced in Korea as early as the 1970s mostly at foreigner-invested companies. But it was not maintained in the country due to lack of institutional preparation and appropriate environment (Korea Chamber of Commerce & Industries, 2007). The causes of failure of job-based pay in Korea at the time can be summarized as follows:

1. Challenges in defining the job grade at the head office, branch offices, planning department and other departments.
2. Rigidity in workforce operation due to fine segmentation of jobs.
3. Workers’ anxiety over slow promotion within the same job.
4. Union’s opposition out of the sense of egalitarianism unique to Korea.

There is still a growing interest in job-based wage system as an alternative to seniority-based pay, but realistic obstacles persist such as inadequate preparation and lack of awareness. Companies cite difficulties in job evaluation and lack of market wage as the biggest obstacles against introducing job-based pay. Adopting job-based pay requires evaluation and scoring of all the jobs inside an organization. The job values should be then linked to specific wage levels in accordance with market wage. But businesses find it difficult to perform such evaluation.

III. Direction of Wage-Structure Reform by Industry and Occupation

1. Overview of Status (Survey) and Case Studies

Survey and case studies were undertaken in parallel between August and October 2013 to identify directions for improving the wage structure for bank office workers, hospital nurses, and auto/parts production workers. Survey respondents and case study subjects were quota-sampled based on the characteristics of wage structure by industry and in consideration of cost and time. Thus, statistical generalizability is limited. In the case of banks, those that are purely private, purely public, and both public and private were surveyed, as were labor and management groups, given that their wages are determined through industrial bargaining and that they have public or private nature.. In the case of hospitals, tertiary hospitals, general hospitals, hospitals, and 3public health centers were all included to reflect different characteristics by size (large, medium, and small) as well as public and private nature. In the case of automakers, finished automakers and primary and secondary parts suppliers were included given the affiliation of their companies.

Survey respondents were the labor and management of 4 banks, 46 hospitals, and 40 automakers and parts suppliers. Case studies were conducted with the labor and management organizations of the banking industry and for 3 banks, 4 hospitals, 1 automaker, and 2 primary and 1 secondary parts suppliers.

2. Summary of Status (Survey) and Case Study Results

A. Retirement System and Workforce Aging

In all three industries, the retirement age was mostly 58 (60 in some cases), making it unlikely that the introduction of a mandatory retirement age of 60 in 2016 will have a big impact in terms of extending the working life. And in all three industries, over-50 workers make up less than 20% of the workforce, indicating that workforce aging for them is not yet a serious problem.

Table 8. *Retirement System and Workforce Aging Survey and Case Studies: Summary of Results*

	Results of Survey and Case Studies
Retirement system	<ul style="list-style-type: none"> ○ Retirement age is mostly 58 (in the case of single retirement age). <ul style="list-style-type: none"> • Banks 58.0, hospitals 58.3, and auto/parts 58.3. ○ Similar results were found in case studies: 60 for all banks; 60, 60, 60, and 58 for hospitals; 60, 60, 58, and 58 for auto/parts makers. <ul style="list-style-type: none"> • At one hospital, labor and management had recently agreed to move the retirement age from 57 to 60 following passage of the legal amendment.
Workforce aging	<ul style="list-style-type: none"> ○ The share of over-50 workers is 19.7% at auto/parts makers, making them the oldest among the three industries. <ul style="list-style-type: none"> • Banks 10.0%, hospitals 13.9%. ○ With regard to the seriousness of the workforce aging problem, most respondents gave a score of less than 4, indicating that it is not felt to be serious. <ul style="list-style-type: none"> • 4 = "Workforce aging is perceived to be a serious problem."

B. Wage and Job Structure

The wage structure in most workplaces except for small auto parts suppliers is based on step pay, indicating the possibility of some conflicts between labor and management when attempts are made to revise the wage structure. In addition, the wage structure and job structure are administered separately for competency-based pay and job-based pay, which might negate the effect of the revision of the wage structure.

In the case of job-based pay, the base wage is often determined not only by the single criterion of job value but also by the element of competency. Before competency-based or job-based pay is introduced, a set of fair and objective standards trusted by both labor and management should be established. On the other hand, a culture that combines work, competency, and performance criteria is already established to a certain extent, as it is often customary to consider not only years in service but also skills and performance when determining promotion.

Table 9. *Wage and Job Structure Survey and Case Studies: Summary of Results*

	Results of Survey and Case Studies
Wage and Job Structure	<ul style="list-style-type: none"> ○ Whereas step pay is used at over 90% of banks and hospitals, it is used at only 65% of auto/parts makers. <ul style="list-style-type: none"> • This is believed to be because 32.5% of parts suppliers are small, employing fewer than 100 workers. • In case studies, production workers at automakers and primary parts suppliers were all subject to step pay, while at secondary parts suppliers they were paid by the hour, without a formal wage scheme. ○ In over 50% of the cases, the inter-step pitch (the slope that indicates the rise in wage according to higher step) increases. In the case of hospitals and auto/parts makers, in 10% of the cases the inter-step pitch either fell or fell after an increase. <ul style="list-style-type: none"> • Inter-step pitch increasing according to rising step: 50.0% at banks, 57.1% at hospitals, 73.1% at auto/parts makers. • Inter-step pitch decreasing according to rising step: at hospitals only, 2.4%. • Inter-step pitch decreasing after an increase according to rising step: 11.9% at hospitals, 7.7% at auto/parts makers. ○ Cases where competency-level management and job are separated under competency-based pay: 62.5% of hospitals, about half of auto/parts makers. ○ Under job-based pay, in over 70% of cases, a promotion occurs when a worker's competency level increases, even when he or she remains in the same job. ○ The biggest reason for not using job-based pay is the difficulty of implementing job evaluations and personnel movement. <ul style="list-style-type: none"> • Often the lack of a job-based market wage makes it difficult to introduce job-based pay; that this is not a problem at hospitals hints that there is a market wage for nurses. ○ In 30% to 40% of the cases, promotion was based on more than just years in service; for the rest, years in service was an important criterion in determining promotion. <ul style="list-style-type: none"> • Cases where performance evaluation is considered along with years in service and where exams are taken for promotion: 32.6% for hospitals, 32.5% for auto/parts makers.

C. Response to the Extension of the Retirement Age to 60

To respond to the extension of the retirement age to 60, or to guarantee employment until retirement age and to improve job security, what is needed for the short term is to introduce the wage peak system and for the medium to long term is to improve the wage structure. In setting the wage reduction rate under the wage peak system, it would be better to consider a variety of schemes such as a rising or flat type, rather than a single, reducing type, taking into account job rotation, competency, and performance evaluation. The types of wage

reduction rate under the wage peak system include rising, slowing down, flattening, gradually falling, falling then rising, and falling then flattening.

Table 10. *Survey and Case Studies on Extension of Retirement Age to 60: Summary of Results*

	Results of Survey and Case Studies
Measure to Prepare for Retirement Age Extension to 60	<ul style="list-style-type: none"> ○ Implementation of the wage peak system was much higher at banks than at hospitals or auto/parts makers. <ul style="list-style-type: none"> • Banks 75.0%, hospitals 4.3%, auto/parts makers 7.5%. • In case studies, one primary parts maker had implemented a flat wage peak system whereby a worker would perform the same job from a certain age until retirement at the same wage level; one bank placed employees subject to the wage peak in other jobs. • In case studies, banks showed a very large wage drop per year, paying less than 50% 4 to 5 years after becoming subject to the wage peak system (bank A 50%, bank B 30%, bank C 10%). ○ Regarding the labor costs accompanying the extension in retirement age, both labor and management at auto/parts makers did not expect it to be burdensome, while at hospitals the management and at banks the labor side expected the cost to be burdensome. <ul style="list-style-type: none"> • “Extension in retirement age will cause considerable burden in labor cost”: banks (management 25.0%, labor 50.0%), hospitals (management 46.0%, labor 21.4%), auto/parts makers (management 15.0%, labor 8.1%). ○ Of the measures to prepare for the extension, both labor and management in all three industries commonly believed the wage peak system to be the first option, although to varying degrees. <ul style="list-style-type: none"> • Measures to prepare for retirement-age extension: introducing the wage peak system, improving step pay, introducing a job-based pay scheme, changing the promotion-by-years-in-service scheme, introducing an individual-performance pay scheme, introducing a profit-sharing scheme. • Perceiving a need to introduce the wage peak system as a way to prepare for the retirement extension: banks (management 75.0%, labor 75.0%), hospitals (management 52.2%, labor 26.1%), auto/parts makers (management 50.0%, labor 52.5%). ○ Labor was found to be less receptive toward all six options presented as preparation for retirement extension.

IV. Wage-Structure Model by Industry and Occupation

This section summarizes the models for improving the wage structure for bank office workers, hospital nurses, and auto/parts production workers identified through the survey and case studies. The models are differentiated by the calculation basis for base wage, mechanism

of wage increase, design of the lifetime standard wage curve, and other factors. The following is a review of the findings.

1. Bank Office Workers

First, the wage peak system has already been implemented relatively broadly in the banking sector. Because it is more common to retire through such channels as “honorary retirement,” the extent of wage reduction under the wage peak system is quite large; however, this has never been an issue. Given that the retirement age will be legally guaranteed to be 60, however, labor is demanding changes to the current system, which is designed for large wage cuts. But this has only exacerbated the differences in stance between labor and management. For employers, the retirement age also existed in the past, but they could not accept the seniority-based pay component that raises the wage level until the time of retirement. This reality does not change even with the new legal amendment, and employers may instead face growing labor-cost pressure due to the additional labor costs for 3 years. The additional burden makes it likely that employers will try to encourage retirement before the statutory age, through such channels as honorary retirement. What is needed for the banking sector is to partially improve the wage peak system and for labor and management to compromise on a set of solutions that would better suit it to the new reality. One example would be to change the peak age to around 57. However, even then, the wage peak system would likely remain only a temporary solution to retirement extension because labor would still find it hard to accept a stronger performance-based pay component in the compensation scheme (preferred by management).

Second, labor today remains negative toward employers’ demand to link performance to the wage structure, but is also reconsidering the validity of basing the wage level for banks’ high-paying jobs on seniority. Thus it is likely that labor will try to reach a compromise by strengthening the variable component in the collective performance incentive. An individual-performance incentive is not likely to be accepted by labor but might be tried for executives.

Third, labor and management agree that the wage gap between regular and non-regular workers in the financial sector is too large. There is a general consensus that the gap cannot be overcome through seniority-based pay, and that fair application of job-based or skill-based pay would be a better solution. But the possibility for actual application should be

sought not for the current generation but for the next generation. The ultimate solution would be to implement job-based pay, whereby wages are based on the value of the job and the resulting performance, even past the age of 50.

2. Hospital Nurses

First, the compensation scheme for nurses has a strong element of supra-corporate market-based wages. It is often the basis for determining pay in other jobs in the hospital such as technicians, and labor mobility between hospitals is quite high. At the same time, there is a high level of interest in the amount paid in other, similar hospitals (to prevent nursing-staff turnover), and there is a strong demand for wage information. This means that there is room for a job-based wage scheme.

Second, there is a pattern of nurses not staying until retirement age. Over 90% of nurses are women, who have a high-level educational background and experience frequent mobility to and from workplace and career. Thus there is less demand from both labor and management for a wage peak system with a retirement-age guarantee; rather, there is more interest in a fair market wage. There is a seniority-based order according to the pay-step table, but in practice wage increases are more typically based on skill level.

Third, hospital labor and management have also explicitly rejected job-based or performance-based wage structures in their bargaining agreement, which also states that changes in wage structure must be mutually agreed on. The designation “job-based” in this case appears to refer to a micro-level job that can be linked to performance. The industrial union cannot simply oppose job-based or occupation-based pay in a broader sense, because these actually represent the possibility of establishing a fair wage structure through workers’ solidarity.

3. Production Workers at Auto Manufacturers and Auto Parts Makers

First, the labor market for these workers is somewhat distorted, and is characterized by low base wages and numerous types of allowances. It also has a dual structure: the automakers have a seniority-based pay scheme, whereas the parts suppliers more often have a job-based wage structure. Under this structure, there is high anticipation of retirement extension among workers at automakers and primary parts suppliers, and some movements to

even reject the existing wage peak system. There is less interest in introducing more rational improvements in the wage structure following the retirement extension.

Second, it is still necessary to create a market-type job-based pay for production workers at SMEs and parts makers where higher performance or productivity will result in higher pay. In light of the potential resistance from labor, this pay should take the form of group incentives, with elements of individual incentives to be added over time.

Third, it is necessary to ensure that seniority and job descriptions are reflected fairly in the wage structure using the skill-based scheme. This will bridge the gap between automakers and parts makers and enable uniformity in the wage structure between them under the principle of “equal work, equal pay.”

As explained above, the wage-structure improvement model should be largely based on revising the seniority-based component and adding other elements, but it is inevitable that different characteristics will be reflected depending on the industry and occupation. Thus the models have been designed based not on the industry as a whole but on the best-known occupation for that industry.

Skill-based pay may be determined differently by industry and occupation, but basically it reflects a diversity of factors such as education, experience, years in service, and qualifications. And it is premised on the assumption that specific skill grades will be agreed on between labor and management (through collective bargaining or a labor–management council).

The wage-structure reform model by industry presented in Table 11 is more like a sample or a template, which can be modified or altered by industry or workplace through case studies or consulting. Meanwhile, the wage-increase patterns for each model can be illustrated using standard lifetime wage curves.

Table 11. *Wage-Structure Reform Model for Bank Workers, Hospital Nurses, and Auto/Parts Production Workers*

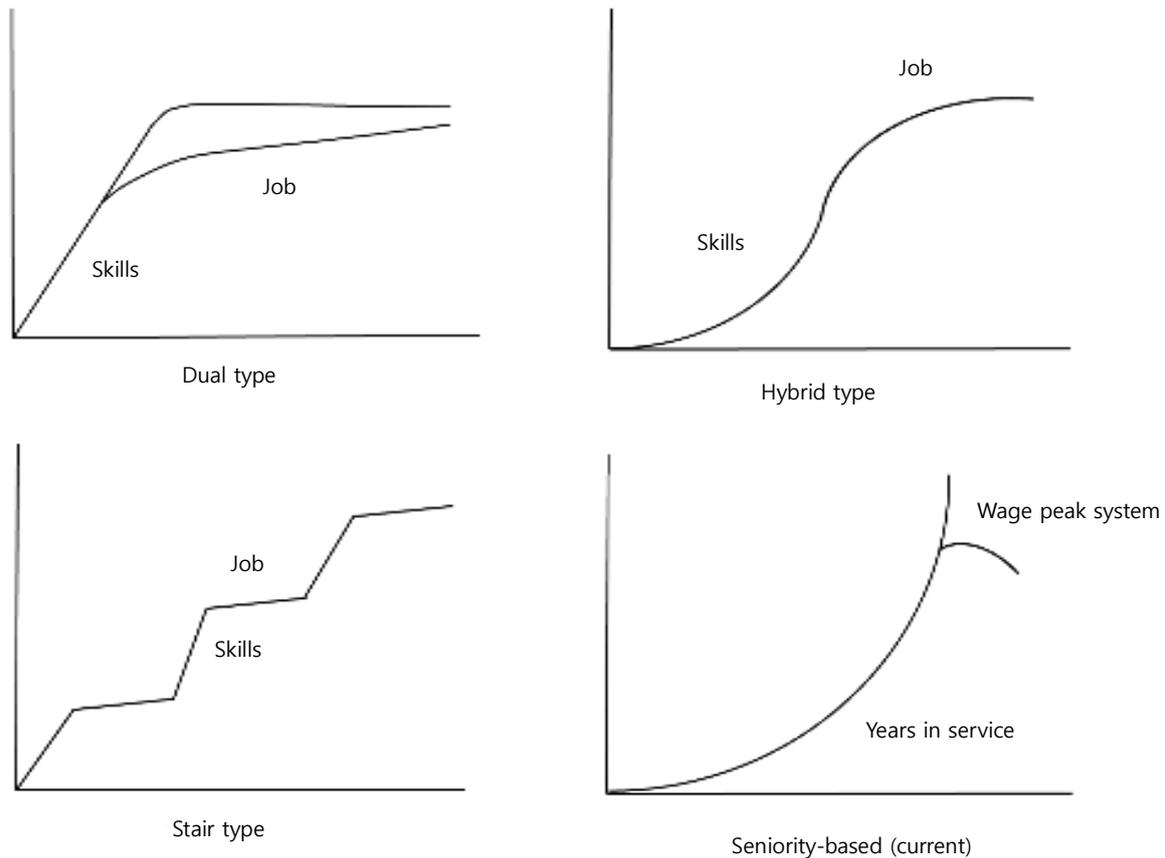
Bank office workers	Hospital nurses	Auto/parts production workers
Characteristics of industry, occupation		
<ul style="list-style-type: none"> • Government’s protection of monopoly/oligopoly in the banking sector has restrained excessive competition and established a relatively stability-seeking culture. • Wage peak system exists in name only because of seniority-based pay structure, high wage level, “honorary retirement.” 	<ul style="list-style-type: none"> • There is a market price for initial salary. • Job allocation and labor mobility are determined by skill level. • High level of interest in and convergence of wage level in same occupations. • Market exit before the formal retirement age is common; presently suffering from labor shortage. 	<ul style="list-style-type: none"> • Low base wage, high overtime pay. • Dual scheme: seniority-based compensation at automakers, job-based compensation at parts makers. Significant wage gap. • Large companies can extend retirement without wage peak system; SMEs find it challenging to guarantee retirement age.
Suggestions for overall improvement		
<ul style="list-style-type: none"> • Short term: promote the use of wage peak system (focus on job development and adjust the extent of wage cut). • Long term: switch to “dual ladder” with role-focused skill-based pay for non-specialized jobs and job-based pay for specialized jobs (around the age of 40). • Improve on the seniority-based component by introducing skill-based component until age 40. 	<ul style="list-style-type: none"> • Short term: improve and disseminate information on market wage. • Long term: use job/occupation-based compensation as the basis, with added elements of skill-based pay. • In consideration of labor shortage, introduce a wage structure for specialized jobs by encouraging broader job allocation and rotation for older workers. 	<ul style="list-style-type: none"> • Short term: to trade off between retirement extension (through job rotation) and wage peak system at automakers. • Long term: to introduce an S-shaped wage scheme. Current seniority-based (at automakers) and job-based compensation (at parts makers) should be switched to skill-based pay that includes performance elements; when productivity starts to fall (mid/late-40s) they should receive job-based pay that is determined by the job’s difficulty level.

Bank office workers	Hospital nurses	Auto/parts production workers
Determining the wage level		
<ul style="list-style-type: none"> • Base pay should be skill-based, then diverge into role-based and job-based pay after the mid-point. • Pay raise should be determined by skill (in skill-based pay), position (in role-based pay), and job (in job-based pay), with differences based on competency and performance. 	<ul style="list-style-type: none"> • Base pay should be occupation-based with skill elements, to be switched to job-based pay for older workers. • Pay raise should be determined by skill or competency improvement such as earning of certificates (in occupation-based pay), or change in jobs or positions (roles) in job-based pay. 	<ul style="list-style-type: none"> • Base pay should be skill-based. For automakers, the existing seniority-based compensation, and for parts makers, the single job-based scheme, should be improved. Commonly for both, job-based compensation (reflecting skill level) should be applied from the mid-40s on. • Pay raise should be determined by skill upgrade in skill-based pay, and job rotation and skill upgrade in job-based pay. Performance difference should be partially reflected.
Reflecting performance elements		
<ul style="list-style-type: none"> • Employees (union members) = group incentive • Executive level = individual incentive • Around 30% of total wage 	<ul style="list-style-type: none"> • Staff nurses (union members) = group and individual incentives • Over middle-aged = individual incentive • Around 20% of total wage 	<ul style="list-style-type: none"> • Before mid-40s = group incentive • After mid-40s = individual and group incentives • Around 10% of total wage
Wage curve		
<ul style="list-style-type: none"> • Dual ladder 	<ul style="list-style-type: none"> • Step-by-step rising curve 	<ul style="list-style-type: none"> • S-curve (hybrid)
Priority issues		
<ul style="list-style-type: none"> • Redefine the wage peak system 	<ul style="list-style-type: none"> • Improving/providing wage information 	<ul style="list-style-type: none"> • Job comparison between automakers and parts makers

The core idea illustrated in Figure 3 is that the wage structure should be simple yet flexible enough to vary depending on a worker's life stage. For example, rather than declaring seniority-based pay to be the answer for the public sector because in that sector there is no market competition, perhaps for the first 10 years a general skill upgrade ensured by seniority-based compensation would be better, but after age 40, more specialized career development would be necessary to guarantee working until retirement age, for which job-based pay would be better suited. In this case, there should be little pay raise to accompany a promotion, but the initial wage should be higher than for non-specialized jobs. And in non-

specialized jobs, whereas a wage increase would automatically accompany a promotion in title or grade, such a promotion should be determined by competition rather than by seniority.

<figure 3> Standard lifetime wage curves



Among the different standard lifetime wage curves, the dual type is applicable to bank office workers. Wages would increase with skill upgrades in the early stage; after a worker reached middle age there would be a separate track for job-based pay whereby the base wage is determined by the job (which would be the specialized job track). In comparison, the non-specialized track would feature continuous wage increases with higher skills and promotions, but in the last stage the wage gap between the non-specialized and the specialized tracks would be reduced because of the wage peak system.

The stair type is a standard wage curve that is suitable for hospital nurses. Wages are based on skill level, but once a job is given to work in a certain hospital, a nurse would

follow a job-based compensation scheme, receiving a slight pay increase with each year at the same workplace. The real wage increase would come when the nurse moved to a new job at a new workplace, through which he or she would be recognized for his or her skills in the labor market in general.

The hybrid type applies to auto and parts production workers. Early in their career, their wages rise with skill upgrades; later, their wage growth slows under the assumption that they have upgraded their skills gradually rather than markedly improving their productivity (S-curve). The wage curve of the hybrid type is different from that of the current seniority-based pay (the last diagram), but it can be taken as a standard type even though not all workers in each industry or occupation show the same curve; the slope or the peak can vary slightly by workplace or worker.

V. Wage Structure Reform and Labor Market Flexibility

This flexibility in wage structure is a mechanism to compensate for the lack of flexibility in employment structures in Korea. The Korean labor market is marked by high dismissal costs, an inadequate social safety net, and a lack of employment flexibility; thus labor and management should try to ensure flexibility by implementing a flexible yet predictable wage structure that can be applied fairly throughout an employee's working career. Seen from this light, the wage peak system rigidly pulls down wage levels at the end of a seniority-based wage structure according to which one's pay increases rigidly. Wage rigidity becomes stronger because the job rarely changes over time. This means that flexibility in the wage structure should be premised on job changes or on development throughout an individual's working career.

As debates and controversies rage on regarding how to improve the labor market structure, there is a growing need to assess the current direction of labor market reform from broader perspective. In this debate, the wage scheme has once again emerged as a chief policy task because today's challenges involve not only extending the retirement age but also reducing the wage gap.

There is a serious wage and income gap among Korean workers. The wage inequality

between regular and non-regular workers has become an important issue in the Korean society. The *2013 Survey on Work Status by Employment Type* revealed that non-regular workers' monthly pay is only 53.3% of regular workers'. The hourly fixed-pay is only 73.5% of regular workers'.

To reduce the gap, the principle of “equal pay for equal work” should be applied at the occupational or job level regardless of the company. In Sweden, the union led the move toward solidarity wage policy that ensures a similar wage level by the job or job type by going beyond the boundaries of companies or industries that inevitably have differences in productivity or financial capability

If the principle of equal pay for equal work, the rule of thumb for solidarity, is to be accepted as the norm in the labor market, we need to reshape the labor market to make it less fragmented and to ensure that the wage is determined by the value of the job performed.

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