

Financing Vocational Training to Meet Policy Objectives: Sub-Saharan Africa

Table of Contents

Financing Vocational Training to Meet Policy Objectives: Sub-Saharan Africa	1
Preface.....	1
Abbreviations and Acronyms.....	1
Executive Summary.....	2
1 General Introduction.....	13
1.1 Background.....	13
1.2 Training Finance: Consensus from the Literature.....	14
1.3 Approach and Methodology.....	16
1.4 Coverage.....	17
1.5 Plan of the Paper.....	18
2 Conventional Patterns of Financing Training.....	18
2.1 Typology of Financing Burdens.....	18
2.2 Shortcomings of Conventional Training Financing.....	20
2.3 Changing Roles for the State, Enterprises and Individuals.....	21
3 The Role of the State in Financing Training.....	21
3.1 Rationale for Government Intervention.....	22
3.2 Designing Appropriate Policy Interventions.....	24
4 Finance Flows: Three Scenarios.....	24
4.1 Conventional Training Markets.....	25
4.2 Training Markets with State Intervention.....	26
4.3 Integrated, Demand-Driven Training Markets.....	28
4.4 The Pace of Reform.....	29
5 The Development of National Training Funds.....	29
5.1 Origins and Objectives.....	29
5.2 Range of Activities.....	30
5.3 Income Sources.....	31
5.4 Disbursement.....	32
5.5 Governance, Control and Stakeholder Representation.....	34
5.6 Sectoral Funds.....	36
5.7 From Training Funds to National Training Authorities.....	37
5.8 Training Fund Sustainability.....	38
5.9 Lessons for Policy: Identifying Good Practice.....	39
5.10 Training Funds in Selected SSA Countries: Organization, Funding Source and Objectives.....	41
6 Training Levies.....	44
6.1 Alternative Training Levy Schemes.....	44
6.2 Payroll Levies: Revenue Generation.....	45
6.3 Levy-Grant Schemes.....	45
6.4 Payroll Levies in SSA.....	47
6.5 Rationale: The 'Benefit Principle'.....	48
6.6 Coverage.....	49
6.7 Levy Income Generation.....	49
6.8 Payroll Levies: An Over-Sheltered Source of Funding?.....	52
6.9 Lessons for Policy.....	53
7 Finance Mechanisms: Augmenting Funding for Training.....	54
7.1 Funding Augmentation v. Funding Distribution.....	54
7.2 Funding Diversification: Alternative Approaches.....	55
7.3 Fund Augmentation.....	56
7.4 Cost Sharing.....	56
7.5 Income Generation by Providers.....	58
7.6 Encouraging Private Provision.....	59
7.7 Role of Government: Four Intervention Modes.....	60
7.8 Responding to Budgetary Pressure: Institutional Income in Tanzania.....	61
7.9 Lessons for Policy.....	62
8 Funding Distribution: Transfers to Training Institutions.....	63
8.1 Direct Allocation Mechanisms.....	63
8.2 Indirect Allocation: Trainee-Based Funding.....	66
8.3 Policy Reform.....	68
9 Enhancing Enterprise Training.....	68
9.1 Direct Training Subsidies.....	68

Table of Contents

<u>Financing Vocational Training to Meet Policy Objectives: Sub-Saharan Africa</u>	
<u>9.2 Levy-Grant Schemes</u>	69
<u>9.3 Indirect Subsidies: Company Tax Concessions</u>	70
<u>9.4 Other Measures to Promote Enterprise Training</u>	71
<u>9.5 Lessons for Policy</u>	72
<u>10 Financing Informal Sector Training</u>	74
<u>10.1 The Informal Sector: a Vehicle for Employment Growth</u>	74
<u>10.2 Developing Informal Sector Training Markets</u>	74
<u>10.3 Funding Informal Sector Training in SSA</u>	75
<u>10.4 Policy Dilemmas in Financing Training for the Informal Sector</u>	78
<u>11 Financing Mechanisms: Contribution to Broad Policy Objectives</u>	78
<u>12 Lessons for Policy: Conclusions and Overview</u>	85
<u>12.1 Major Policy Messages</u>	85
<u>References</u>	90
<u>Endnotes</u>	93

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Preface

The World Bank is currently undertaking a comprehensive study of post-basic education and training in Sub-Saharan Africa (SSA). This project reviews performance of the lending portfolio, explores individual country studies, highlights and assesses sector issues, and draws together international and regional experience that will form a knowledge base for dialogue between the World Bank and its clients. This present study on the financing of training in SSA forms a part of that overall review. A general synthesis of the review is provided in Johanson (2001b).

The main objective of the paper is, through in-depth analysis of current training financing methods and institutions in SSA countries, to derive policy messages that may lead to better practice. The paper provides a logical progression from more theoretical and conceptual issues in the early chapters to a more applied treatment of major financing mechanisms, relating to SSA experience in training finance, in the later ones. Although there is an underlying continuity in theme across the chapters, each chapter has been designed to be self-standing and may be read independently; however, this inevitably has resulted in a certain amount of repetition of material across chapters.

In preparation for this paper three short field studies were conducted in South Africa, Tanzania and Zimbabwe in early 2001; the findings of these visits, and lessons learned, are reported at relevant points in the development of the paper. Given the detailed nature of the material and the in-depth treatment of the major topics, of which references to case studies and individual country practice constitute an integral part, summary tables have been prepared, presenting much of the information and findings in readily digestible form. And, as appropriate, the practical chapters (Chapter 5 through 10) conclude with policy-oriented summary sections, aimed at providing some practical advice for policy, including such issues as what measures work well, advantages and weakness of policy alternatives and pitfalls to be avoided in implementation. Chapter 11 deals with the interplay between national training policy objectives and the main mechanisms for training finance. The final chapter, which serves as a concluding section to the paper as a whole, brings together the main policy messages of the paper.

Many individuals and institutions have contributed, directly or indirectly, to this paper. In particular, I would wish to acknowledge the help afforded to me, in conversation and through their writings, by the following individuals (listed alphabetically): Amit Dar, Lindsay Falkov, Jutta Franz, Ewald Gold, Richard Johanson, Jon Lauglo, Paud Murphy, Thyra Riley and Daniel Viens. Amit Dar and Ewald Gold also provided helpful comments on the draft version of the paper (June 2001). Richard Johanson combed through the draft and revised versions of the paper and offered numerous suggestions for improvement, both in substance and presentation. Very helpful feedback on an early version of the paper was received from participants at the seminar on Development of Post-Primary Education in Africa, held at the Institute of Development Studies, University of Sussex, in the summer of 2001. Amir Ben-David's professional hand produced the charts.

A.Z.
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Abbreviations and Acronyms

CINTERFOR Inter-American Centre for Research and Information on Training

CNFTP	National Council for Technical and Vocational Training (Madagascar)
CVT	Continuing Vocational Training tax (Cote d'Ivoire)
DIT	Directorate of Industrial Training (Kenya)
DTEVT	Department of Technical Education & Vocational Training (Zambia)
FDFP	Vocational Training Development Fund (Cote d'Ivoire)
GTZ	German Agency for Technical Assistance
ILO	International Labour Office
IND	Industrial training board
INTEP	Integrated Training for Entrepreneurship Promotion (Tanzania)
IVTD	Industrial and Vocational Training Board (Mauritius)
MoHET	Ministry of Higher Education and Technology (Zimbabwe)
MSTVT	Ministry of Science, Technology and Vocational Training (Zambia)
MVTTC	Morogoro Vocational Teachers Training College (Tanzania)
NACVET	National Coordinating Committee for Technical and Vocational Education and Training (Ghana)
NVTD	National Vocational Training Division (Tanzania)
NRF	National Revenue Fund (South Africa)
NSSF	National Social Security Fund (Tanzania)
NSA	National Skills Authority (South Africa)
NTA	National training authority
PCO	Project coordination office
RVTSC	Regional Vocational Training and Service Centre (Tanzania)
SARS	South African Revenue Service
SETA	Sector Education and Training Authority (South Africa)
SSA	Sub-Saharan Africa
TAP	Traditional Apprentice Programme (Zimbabwe)
TEVETA	Technical Education Vocational and Entrepreneurship Authority (Zambia)
TRA	Tax Revenue Authority (Tanzania)
VET	Vocational education and training
VETA	Vocational Education and Training Authority (Tanzania)
ZIMDEF	Zimbabwe Manpower Development Fund

Executive Summary

There is now considerable agreement on what are the major ingredients for success in national training policy. For national training systems successfully to achieve the aim of meeting the skills needs of the economy, society and of individuals, five factors should be present:

- **Effective:** offering meaningful, quality skills development, avoiding time-serving and non relevant training
- **Efficient:** avoiding high cost, inefficient provision
- **Competitive:** to counter supply-driven training tendencies and facilitate the development of training effectiveness and efficiency
- **Flexible:** technically able in the short term to change the scope and direction of outputs – training provision – if necessary
- **Responsive:** designed to be responsive to the changing demands of the market and needs of the economy.

A central theme of this paper is that training finance mechanisms, in addition to supplying funding for the national training system, also have a central role to play in achieving these overall policy objectives.

Challenges to Conventional patterns of Financing Training

Traditionally, the direct burden of financing training has fallen, alone or in concert, on the triad of the trainees themselves, on enterprises and on the state.

Today, as in the past, the vast majority of employment across SSA countries is to be found within small scale, informal sector enterprises. Initial training for the informal sector took place on-the-job, within the context of the traditional, unstructured apprenticeship, with trainees (or their families) bearing the costs of training in the form of an initial lump-sum payment and/or a low (apprentice) wage. A different financing pattern is displayed for formal sector training. Where enterprise training provides general, transferable skills, the trainee-apprentice bears the cost of training implicitly through low wages. To the extent that training is not freely transferable, the enterprise assumes some of the burden of financing initial training. Training in pre-employment skills acquired at private markets at proprietary training institutions, is paid for by students.

The above forms of training take place within private markets and are essentially demand-driven, focused on meeting market demands for skills. In nearly all SSA countries public training systems have been established, in parallel; they constitute the leading supplier of structured, pre-employment training, frequently dominating the market as provider of formal sector training. But the state is also a major financier of pre-employment training; courses at public training sectors are either provided free or at purely nominal fees.

This simple financing framework, still current in many SSA countries today, has become inadequate to meet society's skill development needs. A number of emerging trends, including those listed below, have rendered this framework increasingly outmoded:

- An increasing problem in many training systems is a tendency to market failure, with firms under-training in transferable skills, both in terms of the amount of training provided and its quality. The consequent shortages of well-trained, skilled workers in the formal sector, stunts productivity growth, competitiveness and industrial development.
- Ongoing technological change, structural adjustment policies, new and changing patterns of trade and competition, and globalization have combined in many SSA countries to create the need for a much more flexible and responsive training system for the modern sector, than has been manifest in more protected regimes in the past.
- Fiscal restraint is a central feature of structural adjustment policies. Increasingly, limited public sector budgets have seriously constrained the ability of governments to provide adequate and stable funding to the public training sector. In other economies, parsimonious public budgets result from the heavy reliance on revenues from indirect taxes and broadening the tax base may not be feasible
- In many SSA countries, demographic change and high population growth rates have resulted in very substantial increases in the numbers of labor force entrants. The result has been high unemployment, underemployment and low wages, especially for a country's youth. Since modern employment sector remains small and stagnant with little growth potential, an

expanding urban informal sector is being seen increasingly as a major source of manpower absorption and employment growth.

- There is currently an increasing social awareness (and conscience) concerning the low current status and skill needs of special groups, such as the poor, ethnic minorities and women. In parallel, there is a wider acceptance that the government has an obligation to assist in this field, through financing and perhaps skills provision; these developments are likely to be constrained by lack of available government funding, indicating an appropriate role for donor intervention.

In order to meet these challenges, training systems in the SSA region, and the ways in which they are financed, will need to adapt to the new realities. This will require a critical reexamination of the current role of the state, enterprises and individuals in training markets and how these roles will need to change. Directions of change will include the development of private training markets, increased competition between public and private training providers, declining roles for the state in the financing and provision of training, a greater diversification of funding sources for skills development (including enhanced cost recovery, cost sharing and training taxes), encouragement of more and higher quality enterprise training and meeting the special needs of informal sector. These themes are developed in this paper.

Redefined Government Role

Funding mechanisms are aimed, in part, at augmenting the supply of training resources. In conventional training markets it is the state, rather than the direct beneficiaries, that bears the major burden in the financing of training for the formal sector, particularly pre-employment training. These responsibilities have weighed heavily on government, which has reached out to new sources of training finance (either for funding of the current training system or its expansion). But apart from the cost burden, is government funding of training excessive in relation to funding needs? Against the back-cloth provided by a closer look at the factors justifying government financing of training, the issue of defining the appropriate role for governmental intervention in financial training markets may be more readily discussed.

Seven major arguments are often adduced, differentially, to justify a government role in financing and/or provision of training:

- Externalities
- Property rights in human capital, within the enterprise
- Market imperfections
- Inadequate enterprise training
- Weak private training institutional training capacity
- Parity of treatment between trainees and students
- Neglect of disadvantaged groups

The first five arguments lead to under-supply of trained workers; the last two, social arguments are concerned with inequities and the neglect of the needs of the economically weak.

In none of these arguments (except to supplement weak private training institutional capacity) is a case made for state provision of training. The case for public subsidy of training is strongest where externality effects of training are present and in support of skill development programs for disadvantaged groups. The dominant role played by government in both the financing and provision of training is probably excessive in many SSA countries. While there is usually much more public *provision* of training than is required by economic rationale alone, this may not be sub-optimal if public training is efficient, effective and market-responsive; unfortunately, frequently, this is not the case. And again there is far more public *financing* of training than can be justified by the economic arguments alone.

The appropriate role of government in training markets cannot be determined without reference to the capabilities of private training markets. Where they can function well, they can be seen as an alternative to public sector provision; where they do not, then the public sector should be engaged. This approach to the appropriate role of government in training finance and provision requires a country to determine its individual needs for public sector training intervention. It will need to examine the performance of its markets, the capacity of the private sector to deliver training and its own preferences with regard to social policies and equity. On this basis, there is likely to remain a central and continuing role for the state in most SSA countries

in the delivery and, particularly, in the financing of training.

National Training Funds

Training funds have been established in some thirty SSA countries. A national training fund may be seen as a unique institutional framework for unifying and augmenting public sources of funding for training and for allocating funds in line with national policies and priorities. In older established training funds, training levies were the dominant (usually only) income source; newer funds draw from a variety of additional income sources, including government budgetary allocations, donor funding and income generated by the fund itself. Indeed, in some cases training funds derive no income from training levies; either levies have not been instituted or, where in place, levy proceeds are regarded, in practice, as general tax revenues and not passed on to the fund.

Earlier training funds based on payroll levies were largely single purpose – aimed at financing public sector pre–employment training (revenue generating schemes) or at enhancing the amount and quality of enterprise training investment (levy–grant schemes). Some funds had mixed objectives. But in all these cases, levy income was not only committed to pre–designated disbursement targets; there was also a large degree of consonance between those who financed the levy and those receiving the benefits of the training.

With the broadening of training funds both in terms of income sources and the allocation of disbursements, this link has been considerably weakened. Training funds are now increasingly regarded as a general funding pool, distributed across various recipient destinations according to established priorities and policies. This may result in a considerable degree of cross–subsidization of training (such as informal sector training from formal sector levy proceeds).

Disbursement

There are four main destination categories for fund disbursement (funding windows). Each is aimed at distinct client groups (with some degree of classificatory overlap) representing an appropriate response to very different training needs and policy objectives.

- Core funding to training institutions for pre–employment skills development, aimed largely at formal sector employment. Government support of such training at public training institutions is a central element in conventional training markets; similarly, revenue–raising payroll levy schemes are highly supportive of this training.
- Training incentives offered to enterprises in the formal sector where initial training (including apprenticeship training) or continuing training is deemed insufficient. These may take the form of direct training subsidies to companies or training levy reimbursement.
- Training courses for the unemployed and other disadvantaged, either through financing special courses at public training institutions or (preferably) by contracting for the provision of such training, following public tender that is open to both public and private training providers.
- Meeting the training needs of micro–enterprises and the informal sector, where these conventional private markets are not adequate to meet the changing needs of this growing, more technological–based sector.

The range of institutions and training forms eligible for funding support may vary markedly from case to case and are usually designated in the enabling legislation setting up the fund. In many SSA countries, the precarious state of public budgets, combined with limited income generating capacity of payroll levies, will require strict disbursement priorities. The relatively small size of the formal employment sector and its lack of growth, combined with considerable growth potential for informal sector employment, may indicate the need for a different pattern of disbursement priorities than is found in other regions. Developmental needs in many SSA countries are likely to indicate that core finance for pre–employment courses at training institutions, together with innovatory methods of financing training for micro–enterprises and the informal sector, should make first call in terms of disbursement priorities. Whatever the merits of such expenditures, pressures on public budgets are likely to result in the neglect of disadvantaged groups, unless designated funding is forthcoming from donor sources.

Fund Sustainability

An important objective of establishing national training funds (particularly when financed by company training levies) is to provide sustained and stable funding for the training programs they support. In practice this has not always been achieved, notably when funds do not receive the resources that have been designated to finance their activities; training levy proceeds, designated for the training fund, may be absorbed instead into general government revenues. Training fund sustainability over the longer term constitutes a serious problem in some countries, in particular where training funds have been launched by donors and are funded, in the main, externally. This problem of fund sustainability will be endemic in those many SSA country situations where public budgets are likely to be severely constrained over the medium term and where the time is not ripe for the introduction of training levies. In this situation, over-generous external support for national training funds, without the planned, complementary development of domestic funding, will result ultimately in moribund training authorities and empty coffers.

Training Authorities

Where institutionally possible, fully-fledged, autonomous national training authorities should be established, charged with the central role of assuming responsibility for national skills development. To respond to the developing skill needs of the economy and to be in a position to be proactive, rather than just responsive, in relation to ongoing technological and industrial change, public training systems need a greater degree of independence than is forthcoming from line ministries. National training authorities will often play a central coordinating role in planning the national training system, in developing training policy, supervising national skills testing and certification as well as providing necessary information services and developing appropriate labor market signals.

Conditions for Training Fund Success

Successful outcomes are unlikely to be forthcoming unless six key conditions are satisfied.

- Security of income to the fund: assure adequate levels, stability and sustainability of training fund incomes
- Fund management autonomy: ensure decision-making autonomy of management board and its control over budget allocations
- Stakeholder ownership: substantial representation of the major stakeholders on management board, engendering a sense of ownership – particularly of employer groups where training levies are in place
- Restriction of fund activities to national training needs: ensure that training fund policies and disbursements are targeted according to defined national training needs and that extraneous (non-training) activities are avoided
- Avoid role of training provider: training centers run (and financed) by a training fund tend to receive high subsidies and preferential treatment; this distorts training markets and militates against moves towards an open, competitive training system
- Transparency of fund management decision making: decision-making to be open and, in particular, the basis for fund allocation to be known and understood

Training Levies

Earmarked levies on enterprise payrolls have emerged as the most widely adopted funding mechanism for financing training, both in public training institutions (usually under the aegis of a national training fund/authority) and in enterprises. They are central to training-finance policies in many SSA countries others are currently examining the benefits and feasibility of introducing payroll levies to finance training.

The scope for levying payroll taxes is well established by international experience, in SSA countries and elsewhere: almost all countries that have introduced payroll levies have set a standard national levy rate in the range of one to two percent of company payroll bills, the majority at the lower end of the range. Some SSA countries have introduced sector-level training taxes, usually (but not always) based on payrolls; the main advantage is that they offer a means of tailoring the levy format to the specific characteristics and needs of the sector in question. Yet the narrow focus of sectoral levies (and the training funds they finance) obviates an

integrated, national approach to the finance and planning of skills development. This has militated against their broad adoption and most countries have wisely employed standard, national-level levy schemes, based on enterprise payrolls.

Types of Payroll Levies

National payroll tax schemes are usually classified into two distinct groups, reflecting very different underlying objectives: revenue generation schemes (where levy proceeds are used to finance training provided by public sector institutions) and levy-grant schemes (aimed at encouraging training investment by firms themselves). However, this traditional dichotomy is becoming somewhat outdated as evolving levy schemes begin to take on a broader range of tasks, particularly in the context of the development of national training funds and training authorities.

Revenue generation: Levy proceeds are used mainly to support public sector training provision, with the emphasis on initial training at formal public training institutions.

In the SSA context especially, payroll levy schemes of this type may be seen as a mechanism for greater funding diversification, lightening the burden of training funding falling on the state. The expectation that levy income would complement existing government financing, thus providing an additional source of funding, has not always realized in practice, with levy income displacing government subventions. There are also notable cases of the opposite tendency, where 'earmarked' training taxes are absorbed into general government revenues rather than being used for the financing of public training.

Levy-Grant Schemes: Unlike revenue generation schemes aimed at financing training institutions mainly in the public sector, levy-grant schemes focus on company in-service training. They create incentives for a firm to invest more in the skills development of its work force, be it in the sphere of training on-the-job (setting up or extending and improving existing company training) or by sending workers to train externally. The need for government intervention, via the introduction of levy-grant arrangements, arises because of shortcomings in the amount and/or quality of enterprise training. While there are numerous variants, a three-fold classification of levy-grant schemes has been widely adopted – cost reimbursement, cost redistribution and levy-exemption

- Cost reimbursement. The training fund pays grants to firms on a cost-incurred basis, for certain designated forms of training (both on and off-the-job). The purpose of these schemes is often misunderstood, particularly among employers; the scheme aims not at reimbursement of the levy as such but rather reimbursement of training expenditures incurred (to encourage firms to train more or better). Thus a training expenditure reimbursement ceiling (for firms that train to acceptable standards) is usually set, up to a given percentage of the levy paid. This is the variant generally adopted in SSA.
- Cost redistribution. Designed in particular to deal with the ill-effects on training supply of the poaching of skilled workers by non-training firms, the scheme redistributes the burden of training expenditures amongst enterprises away from companies who do not train, towards those who do. Training companies may receive grants far in excess of the amount of levy paid, providing strong incentives for firms to train. There are few examples cost redistribution schemes in the SSA region.
- Levy-exemption. Usually employed as part of broader cost reimbursement schemes, levy-exemption allows firms, adequately meeting their training needs, to withdraw from the levy-grant system or at least to benefit from reduced levy assessments. A major advantage is freeing firms from the bureaucratic fatigues of levy payment and subsequent grant claim – potential cash flow problems are avoided. While much discussed, this mechanism is found more typically in industrialized economies rather than in developing countries.

Advantages and Limitations

It moving towards policy reform, the strengths and advantages of payroll taxes should be set against their possible dangers and limitations.

Advantages of a payroll levies:

- Diversifies the revenue base for financing training, by mobilizing additional revenues
- Can provide a stable and protected source of funding for national training provision; this is particularly important in the context of national budgetary instability
- Where forming part of a levy–grant system, can encourage firms to intensify their training efforts, increase training capacity and raise training quality
- A strong case can be made for viewing earmarked payroll levies as "benefit taxation"
- Training levies collected from formal sector employers can serve as a vehicle for cross subsidization of training, especially from the formal to the informal sector

Limitations:

- Given their particular training needs, many firms, particularly small ones, do not benefit from the scheme; this breeds resentment, opposition and compromises the status of training levies as "benefit taxation"
- Earmarked taxation do not conform well with the principles of sound public finance and weaken attempts to unify the national tax system
- Under fiscal pressure, government may incorporate training levy proceeds into general public tax revenues
- Levy proceeds may be diverted to non–training uses
- Payroll levies may constitute an over–sheltered source of funding, leading to unspent surpluses, inefficiencies and top–heavy bureaucracies
- Payroll levies raise the cost of labor to the employer, possibly discouraging employment
- Employers may shift the incidence of the levy on to workers in the form of lowered wages; in this case, workers and not the employers bear the burden of the tax

Issues in Levy Scheme Design and Implementation

The success record of training levies in SSA countries appears to be less than in other regions. Particular attention will need to be accorded to levy scheme design and implementation in order to secure the benefits of payroll levies while avoiding some of the weaknesses that have been evident in the SSA context. These include the following points:

- Levy rate: levy rates to be subject by law to periodic review to avoid the accumulation of surpluses
- National or sectoral levy rates: a standard, national payroll levy rate (rather than differing sectoral rates) will be most appropriate for most SSA country situations
- Sectoral coverage: levy coverage should be as wide as possible across economic sectors and to include public enterprises
- Company size: very small firms should be exempt from levy payment, on both efficiency and equity grounds
- Levy collection: levy collection should be placed in the hands of effective agents; self–collection by funding organization should be avoided
- Security of levy proceeds: special attention should be given to guarding levy revenues from raiding by the government (especially where tax authorities act as the collection agent), by placing in special, closed accounts

- Employers buy-in: employers should be involved in payroll levy policy formation and execution
- Premature introduction payroll levies: payroll levies may be inappropriate where levy-income generating capacity is weak – either because of the limited size of the formal sector or administrative/organizational difficulties of levy collection

Finance Mechanisms: Augmenting Funding for Training

A central feature, common to virtually all training systems in SSA is the pressing need to augment the total amount of funding for public sector training, in the light of a paucity of government funding – in part the result of the adoption of structural adjustment policies and increasing calls on government funding from competing sectors. The response is greater funding diversification: seeking alternative or additional funding for public training from other sources.

Funding diversification can take many different forms; in particular, four different avenues may be pursued, separately or in combination.

- Fund Augmentation: public sector training funds available for the support of training institutions via subventions, may be augmented from other sources – the classic method is to impose special taxes, earmarked for training.
- Cost Sharing: the weight of training finance falling on public funds may be lightened through the introduction of cost sharing with the beneficiaries of training, mainly in the form of introducing training course fees or by raising them to more realistic levels. These measures will allow a reduction in public subsidies for training or the provision of more or better training services with given levels of public support.
- Income Generation: training institutions may seek additional income from other sources, such as selling of products (combining production with training) or renting out of facilities.
- Private Training Provision: encouragement may be given to the development of private training institutions, thus generating additional funding for training and, in parallel, reducing the call on public funds. This approach is particularly relevant where expansion of the training system is desirable.

The first three approaches act directly in bringing in additional revenues to the training sector while the fourth affects training budgets only indirectly. Of the methods of direct funding augmentation, the first increases the size of the funding pool available for distribution to training institutions, but there is no immediate effect on the income of individual training institutions. Diversification options are not alternatives; all four avenues may be explored simultaneously. However, whether or not to do so and to what extent, remains a policy issue that must be settled within the context of conditions ruling in each country situation.

Fund Augmentation

Earmarked training taxes, levied on the payrolls of enterprises, have emerged as the most widely adopted alternative to central government budgetary allocations for training. Training levies can constitute a stable and protected source of funding for national training provision; in many cases, the declared intention underlying the introduction of a payroll levy is to lighten public sector financing burdens. However, there remains the danger that, due to funding pressures from other areas of government activity, this process may be taken further than desired with levy income replacing, rather than complementing, government funding.

Cost Sharing

Unlike fund augmentation, which results in a larger funding pool, cost sharing aims at reducing the size of allocations to individual training institutions. The best known and most widely used method, is the imposition, or raising the level, of user fees to trainees or students enrolled in training courses.

There is little conformity of practice in tuition fees policy across SAA counties. The feasibility for tuition fee setting (in relation to unit costs of training) is a compound of many and diverse factors; these will vary from

place to place. They include: type and costs of training, the price elasticity of trainee demand for different training courses, political constraints and policies for equality of opportunity. Thus it is not possible to be prescriptive in relation to the scope for generating revenues from tuition fees; this will need to be settled on a case-by-case basis, in the light of local conditions and possibilities.

A central issue in fee policy is whether a regime of standard, national-wide compulsory fees should be instituted or whether freedom should be accorded to individual training institutions to fix the level of fees overall, and differing by type of training course. Institutional autonomy in the setting of fees represents the more desirable approach; it will encourage training providers to develop a more dynamic, even aggressive, approach to exploiting the potential of the local market environment. In this way institutional fee policy becomes more than a device for cost recovery and cost sharing: in providing a mechanism for varying fee levels across courses and client groups it serves as a tool for moving the training system towards an environment characterized by open, demand-oriented training. However, the voluntary setting of user fees may not be feasible in otherwise centralized training systems. While standard, compulsory fee setting may be an inflexible tool, unlikely to reflect local market realities, it is generally acceptable as a second-best measure for reducing pressures on public budgets.

The positive financial benefits from greater cost recovery need to be examined alongside the potentially adverse effects on equity. There is a clear trade-off here. Higher, realistic fees will exclude from training those who are unable to pay; fees set at comfortably low levels will fail to make a sizeable contribution to cost recovery. In particular, negative impacts on the access to training opportunities of the poor, minorities, rural populations and other disadvantaged groups are likely to ensue. This points to the widely recognized need to introduce targeted subsidies directed to these at-risk groups, in the form of scholarships and reduced fees. However, targeting those *most* in need within these groups, particularly in the SSA context, has proved to be no easy matter.

Cost sharing through the use of user fees will discourage participation in formal training programs, even by the non-poor. The classic solution to this problem, encountered most frequently in higher education, is deferred cost recovery in the form of student loans schemes. But the track record for student loans schemes in SSA is poor. The sound administration of a loans scheme requires appropriate, high level, institutional support – at a premium in many SSA countries. Given the lack of success in administering student loans scheme in SSA, it is improbable that training loans would fare better.

Institutional Income Generation

Income generated from the sale of production and service activities of trainees can constitute a useful form of additional institutional income. Income may be derived as a byproduct of the training process itself. But it is possible, more purposefully, to utilize available skills and facilities to produce output for sale in the local market; indeed, exposure to local markets may lead to more relevant, market oriented training. Here the issue is one of maintaining a healthy balance between these two activities. As more weight is given to instruction, the income potential from production declines; alternatively, quality of training will suffer as emphasis is placed on production rather than instruction.

The proportion of recurrent expenses that can be covered by production sales will vary considerably from case to case; the scope for income generating from production will depend on numerous local factors, including the nature of the product, local demand conditions and potential market competition. If an acceptable balance is maintained between training quality and production for sale, the scope for cost recovery may be fairly limited, usually accounting for only a few percent of recurrent expenditure. In some exceptional cases, however, it can contribute a considerable proportion of total costs.

Training institutions may also generate income from the sale of services, including the renting out of underused facilities and providing consulting services to local enterprises.

As with training fee policy, local institutional initiative in income generation from production will be stunted if this income does not contribute to institutional budgets; this is the case where the sums collected are deducted from institutional budgetary allocations and thus accrue to government budgets or the national training fund, and not to the training institution. Institutional fee charging and income generation objectives can be furthered through decentralization of control over public sector providers and greater institutional autonomy. It is only in this more liberal context that the full potential of cost sharing and income generation is likely to be forthcoming.

Encouraging Private Provision

The growth of private training institutions, with trainees paying full costs, provides a pathway for expanding the national training system without heavy commitments of public funds. Indeed, *reduced* public training provision could be possible (and concomitant budgetary reductions) with the reduction in public training supply made up by compensating expansion of private training institutions.

In many countries in SSA, the lack of private training provision results from constraints that hold back the development of private training institutions. These are financial constraints, issues of fees policy, regulation and control of private institutions and information gaps.

- **Financial Constraints:** A lack of capital resources, combined with financial market imperfections, together may constitute a serious barrier to the development of these incipient training institutions, especially for high cost industrial and technical courses. To offset limited capital market access, governments may offer development loans or subsidies, particularly in strategic skill areas, to assist these firms in their start-up phases. Equipment grants and subsidies for staff development may also be warranted.
- **Fee Policy:** Imposed tuition fee ceilings, while aimed at protecting trainees from exploitive activities by private training institutions, may too rigidly limit the ability of these institutions to enter new training markets, especially those with high investment and recurrent costs.
- **Regulation:** Private training institutions are unlikely to flourish in an overly strict regulatory environment. Regulation and enforcement should be sparing; while sufficiently robust to counter dishonest practices and low quality training, they should be designed to encourage private training institutions to operate fairly and efficiently within a facilitating, regulatory environment.
- **Consumer Information:** Without reliable information, consumers are unable to make wise and informed choices. Information on both the quality and stability of private training institutions is often lacking for private training institutions; this may be provided by government. The provision of updated information on the relevance of courses to labor market demands and job opportunities is also important.

Funding Distribution: Transfers to Training Institutions

The allocation amongst training providers of the total government budget for training, is a major component of the financing system in SSA countries. In most cases, a clearly formulated, objective disbursement policy is lacking. A much needed reform is the adoption of moves towards the gradual dismantling of the arbitrary, *ad hoc* institutional core funding arrangements in place in almost all SSA countries, and their gradual replacement by objective funding formula, such as those related to inputs, outputs and outcomes.

These reforms are important because the mechanism through which government transfers funds to training institutions has an important effect on the way in which this funding is used and on institutional behavior more generally. Inherent shortcomings in the transfer mechanisms currently used promote low internal efficiency of training institutions and a strengthening of supply-driven training provision. An important task of funding disbursement policies is to provide an appropriate mix of regulation and incentives to ensure that public training can hold its own in an environment of competitive training markets.

Unlike the case of other desirable training finance reforms, moves towards more objective criteria seem well within the grasp of the governments in many SSA countries and there has been some promising experimentation with these methods in current training institution reform in the region. Barriers to progress stem more from institutional resistance, opposition of vested interests and the slowness of higher education institutions, which would be expected to lead the way here, to move in this direction. But change could well be on the horizon in countries formulating a broader package of institutional reform; objective funding criteria might then constitute part of a more general reform of institutional funding, which would include reduced public funding overall (replaced by cost recovery and income generation), decentralization and enhanced institutional autonomy and a greater use of contact funding.

Encouraging Enterprise Training

A legitimate response to the tendency for firms to under-train is the offer of training incentives to encourage firms to train. These may be provided as:

- direct subsidy of enterprise training out of public funds
- training cost reimbursement, as part of a levy–grant system
- indirectly, through concessions for firms that train, on company tax obligations.

Alternative Forms of Subsidy

Levy–grant systems (where the training grant to the enterprise is financed by a training levy) have some clear advantages over the two alternative incentive systems, direct government subsidy payments and concessions on enterprise tax obligations. A major advantage of levy–grant systems is that they do not draw on public funds, a point of some importance in times of parsimonious government budgets; in addition, they can lead to a more systematic, structured approach to training, rather than a more *ad hoc* one. The central lacuna in training under–provision are not only that amount of training provided is too low, but also that it is often piecemeal and insufficiently well integrated.

The response to direct and indirect subsidy schemes may be low, because they are insufficiently focused to catch the attention of senior management. But in the case of levy–grant schemes, 'involvement' is assured automatically by the compulsory payment of the levy; anecdotal evidence suggests that senior company finance officers exert pressure on the training function to ensure that "we get back the levy", through appropriate training provision.

The disadvantages of tax concession schemes have militated against their adoption in other than a very few SSA countries; they require a well–developed and broadly based system of corporate taxation, often lacking in SSA countries and responsiveness of firms may be low because few firms earn sufficient profits to benefit from tax exemptions.

All three mechanisms share a number of weaknesses. These include:

- Windfalls: Eligible training may have been provided by the enterprise even in the absence of the incentive scheme
- Training Distortions: May bias training towards more formal and externally–provided training, away from informal training on the job
- Repackaging: May lead to the adaptation and documentation of existing training provision to comply with eligibility requirements
- Inspection Costs: The central costs of inspection and monitoring, to counter abuse by enterprises, may be high
- Administrative Burden: The cost to the enterprise of establishing eligibility and compliance (including paperwork and record–keeping) may be considerable

A central problem in training grant design is to minimize the effects of these weaknesses.

Subsidizing Apprentice Wages

In many SSA countries, apprenticeship training is a key method of skills development for the formal employment sector. Support for apprenticeship training, in the form of subsidizing the wages of apprentices, often constitutes part of a wider regime of government training subsidies or levy–grant schemes, as described above. A particular case can be made for subsidized apprenticeship wages on both equity and efficiency grounds.

Apprentice wage subsidies can be a useful tool, positively influencing the quantity of initial training provided by companies; however, for this to be the case, some preconditions must be present:

- that employers do not exploit the availability of apprentice wage subsidies, to gain access to cheap labor
- that the elasticity of supply of apprenticeship slots is not low, in which case the desired supply response of an increased apprenticeship intake will not be forthcoming

- that apprenticeship training on–the–job provides genuine training and skills development for the worker, in turn imposing costs on the firm which are offset (in part or full) by the wage subsidy.

Needs of Disadvantaged Groups

A continuing and enhanced government role in skills development should form an integral part of a package of measures to assist disadvantaged groups. There is an increasing social awareness (and conscience) concerning the low current status and skill needs of special groups, such as the poor, ethnic minorities and women. In parallel, there is wide acceptance of the view that the government has an obligation to assist in this field, through financing and perhaps provision of special programs, aimed particularly at securing entry into the informal sector. These developments are likely to be heavily constrained by lack of available government funding because they are coincident with increasingly limited public budgets and greater inter–sectoral competition for funding allocations. This may indicate an appropriate role for donor intervention.

Financing Informal Sector Training

Central attention needs to be paid to the largely neglected training needs of small micro enterprises and informal sector producers. Throughout SSA countries, considerable population (and labor force) growth, combined with minimal employment increases in the combined public and formal private sectors, place an increasing absorption burden on the informal sector. While traditional informal sector training markets, characterized by non–structured within–firm skills acquisition, continue to serve the sector well, the system is proving too narrow to cope with the increasing challenges emanating from technical change, skills enhancement and the widening of geographical markets. Public institutional training has not been able to adapt to the particular skill needs of the informal sector. Thus an increasingly central role for specialized training providers (external to the firm) is now seen, both for entry training into new skill areas and developing markets as well as for informal sector workers and proprietors; private markets have not been able to fill this void, thus defining a critical role for government initiatives, perhaps buttressed by donor support.

Voucher schemes, though still largely experimental, are operational in a number of SSA countries; they aim at building up consumer demand for training courses for the informal sector and at facilitating a competitive response amongst training providers, through the exercising of consumer choice of training institution and course offering. Vouchers typically do not lighten the financing burden falling on the funding body; training remains subsidized and cost recovery is not an integral part of the scheme (though it may be present). But vouchers can lead to greater cost–effectiveness of training provision, wider consumer (trainee) choice and an improved demand–orientation of training for the informal sector.

Applications to Policy

The reader is referred to the final two summary chapters, where respectively, financing mechanisms are matched with policy objectives, and major policy messages are summarized.

1 General Introduction

1.1 Background

It is now a decade since the World Bank issued its policy paper on training in developing countries (*Vocational and Technical Education and Training: a World Bank Policy Paper*, May 1991), followed by a detailed account of the research evidence on which it was based (Middleton, Ziderman and Adams, 1993). These publications have played a central role, both within the World Bank and outside, in providing a general framework for defining appropriate training policies and projects and in leading to better practice in the field; the finance of training constituted a central theme in this work. However, these publications did not address the needs of specific regions or different levels of development.

This paper provides a more specific study of training finance needs and policies in the Sub–Saharan African regional context. While much relevant case material exists on recent training finance experiences in Sub–Saharan Africa (SSA), this tends to be inaccessibly scattered in project documents and unpublished case studies. This material has never been brought together formally and there has been little updating of this knowledge base. Little evidence has been gathered to assess systematically the effectiveness of funding

innovations in the 1990s. One exception is analytical work carried out by the World Bank and the ILO on vocational education and training in the second half of the 1990s, which included three case studies on reforms in SSA countries, (Gill, Fluitman and Dar, 2000). However, coverage of financing issues in these case studies was scant.

1.2 Training Finance: Consensus from the Literature

Over the last decade or so, there have appeared a number of overviews of issues relating to training finance in developing countries, focusing on both theoretical issues and practice. Major contributions to this literature include the following: CINTERFOR/ILO (1990), Ziderman (1990)¹, Dougherty and Tan (1991)², Ducci (1991), Herschbach (1993), Gasskov (1994), Wallenborn (1994), Bolina (1994), Atchoarena (1996), Gill, Fluitman and Dar (2000), and Jager and Buhner (2000). While a few dissenting voices have been in evidence,³ this literature is notable for the large measure of unity in general approach and conformity in the findings and recommendations of the constituent contributors. In this section we draw together some of the central elements of this 'emerging consensus' and then pose the question: what may be derived from this literature for a better understanding of training finance practice and reform in SSA?

The main elements of this consensus may be presented, in summary form, in the following way. Center stage is given to the overall policy objective of developing an effective, efficient, competitive, flexible and responsive training system that is characterized by demand-driven training, defined as training provision that is responsive to, and aims at meeting, the skills needs of the economy and society and of individuals. Each of these five elements are important ingredients for success. Training systems should be: *effective* (offer meaningful, quality skills development, avoiding time-serving and non relevant training); *efficient* (avoid high cost, inefficient provision); *competitive* (to counter supply-driven training tendencies and facilitate the development of training effectiveness and efficiency); *flexible* (technically able in the short term to change the scope and direction of outputs – training provision – if necessary; and *responsive* (designed to be responsive to the changing demands of the market and the economy).

Financing mechanisms have a central role to play in achieving this overall policy objective.

In particular a reconsideration of the dominant role played by government in the financing and provision of training at public training institutions will be required. A redefined (and diminished, but still critical) government role will entail reduced public budgetary support for formal sector training, accompanied by a diversification of sources of financing, greater cost recovery and cost sharing. Public funding of training institutions would move away from arbitrary, *ad hoc* funding arrangements to objective formula funding related to inputs, outputs and outcomes.

Moves towards increased cost sharing will imply the imposition of higher, more realistic training fees accompanied by scholarships for the needy and disadvantaged groups and perhaps state-backed student loans schemes. More voice would be given to trainee/consumer choice; voucher schemes may provide a mechanism for developing the demand side of the market in those situations where subsidy needs to be retained, at least over the shorter term.

Funding diversification measures include training levies on enterprises and enhanced income generation by public training institutions. Government should encourage and facilitate the growth of private sector provision where feasible; this will provide a desirable, competitive framework for the formal training sector as a whole, leading to more effective, open and cost-effective provision. Government institutional funding should address the need to offer incentives for efficient, market-oriented training, using such devices as output funding and contract training. Funding allocations would be made on a competitive basis, with the aim of raising institutional efficiency, integrating training markets and moving towards demand-driven provision. These objectives would be furthered through parallel policies for the decentralization of control over public sector providers and greater institutional autonomy.

Where formal sector enterprises under-train, levy-grant mechanisms may be seen as useful devices to encourage firms to increase investments in the skills development of their workers. The development of national training funds is an encouraging trend, indicative of a recognition of the need to take a longer term view of training expenditures in a national context. Where institutionally possible, fully-fledged, autonomous national training authorities should be established (or the responsibilities of training funds broadened), charged with the formation and steering of national training policy. Participation of the main stakeholders (especially employers) is important in national training policy formation and management; for example, this may be achieved through providing an active, participatory role for major stakeholders in the governance of

national training funds and training authorities. Participation has an important role to play in building national consensus on training issues; this may be particularly important where training levies are imposed on enterprises.

Attention also would be given to the particular, and largely neglected, training needs of small micro enterprises and informal sector producers. Finally, there should be a continuing and enhanced government role in skills development as part of a package of measures to assist disadvantaged groups.

The fifteen central elements of the emerging policy consensus are summarized in Table 1.1, which follows.

Table 1.1
Training Finance: The Emerging Policy Consensus

Overall training policy objective: To facilitate the development of effective, efficient, competitive, flexible and responsive (demand-driven) Training markets, to meet national economic and social needs and the needs of individuals		
Role of training finance in moving towards this objective	Explanation	Detailed discussion in chapter
Redefined government role	Redefinition of government role (diminished, but still critical), entailing reduced public budgetary support for formal sector institutional training	3
Funding diversification	Diminished state financing is to be accompanied by diversification of sources of funding, greater cost recovery and cost sharing	7
Cost sharing	Moves towards increased cost sharing, with higher, more realistic training fees (with scholarships for the needy) and perhaps state-backed student/trainee loans	7
Training levies	Funding diversification measures to include training levies on enterprises	6 and 7
Income generation	Funding diversification measures also include income generation by public training institutions	7
Decentralization	Income generation objectives would be furthered through decentralization of control over public sector providers and greater institutional autonomy	7
Private sector	Government to encourage private sector provision of training	7
Funding public training institutions	Replace arbitrary, <i>ad hoc</i> funding arrangements by objective formula funding related to inputs, outputs and outcomes. Consider case for subsidy of selected private training institutions	8
Trainee/consumer choice	More voice is to be accorded to trainee/consumer choice; vouchers may help develop the demand side of the market where subsidy needs to be retained	8
Levy-grant systems	Levy-grant mechanisms to be introduced where formal sector enterprises under-train	6 and 9
Training funds	National training funds to be developed, to take a broader and longer term view of training expenditures in a national context	5
Training authorities	Where institutionally possible, fully-fledged, autonomous national training authorities to be established	5

Stakeholders	Increased participation of stakeholders (especially employers) in national training policy formation and execution	5
Disadvantaged groups	Continuing and enhanced government role in skills development as an integral part of measures to assist disadvantaged groups	10
Informal sector	Central attention to be paid to largely neglected training needs of small micro enterprises and informal sector producers	10

1.3 Approach and Methodology

In terms of the focus of the present paper on SSA experience, the usefulness of the available literature is limited in a number of ways. While these reviews often contain good, detailed discussions of individual innovative financing mechanisms, what is lacking is a broad contextual framework and, in particular, a clear discussion of how the various measures relate both one to the other and to the training finance system as a whole. Many contributions discuss different financing mechanisms within defined categories. Thus Herschbach (1993) classifies training finance mechanisms largely in terms of the sources of the funding (through public revenue, enterprise financing, fees etc), an approach closely followed by Bolina (1994). The KODIS report (Jager and Buhner, 2000) categorizes and discusses financing mechanisms in terms of whether training is financed unilaterally (i.e. exclusively by one of the stakeholders, be it the state, employers or trainees) or is co-financed. Dougherty and Tan (1991, 1997) discuss financing according to use (subsidies and other incentives) and also sources of finance.

The approach adopted in the present paper is a rather different one. Initial emphasis is placed on viewing individual financing mechanisms in the context of the system of training finance flows as a whole. Attention is given to the particular, and differing, objectives of these mechanisms. Thus it seems important to distinguish, *inter alia*, between: mechanisms which are primarily aimed at broadening the sources of funding (funding diversification); those mainly concerned with improving the allocation and effective use of funding by training providers; mechanisms aimed at offering incentives for more and better training, particularly enterprise-based training; and those mechanisms designed to improve the overall efficiency of training markets. Since training finance mechanisms ultimately serve to facilitate the achievement of defined policy objectives, towards the end of the paper mechanisms are categorized in terms of the policy objectives they are designed to further; this may provide a background for discussions of the efficacy of different mechanisms for meeting these objectives.

Much of the literature is culled in general, rather than country-specific, terms; to the extent that it does draw on practical examples and detailed case studies these are relatively limited in number and largely drawn from experience outside SSA countries. Thus in their discussion on the international experience with training incentives, Dougherty and Tan (1991) provide sections on Latin America, East Asia and industrialized countries; no SSA cases are discussed, even though well established financing schemes have been in place in some African countries for decades. This treatment follows the general pattern in the literature, where most attention has been given to experience in other regions. In particular, the Latin American experience, in levying company payrolls to fund the building up of national training capacity under the aegis of representative national training bodies, has been well documented (CINTERFOR/ILO 1990, Duchi 1997). Similarly in Asia, for example, the Korean system of training-tax exemption, Singapore's levy-grant scheme and Malaysia's changing funding system have all been closely studied.

But can these practices be applied in the very different African setting? The efficacy of relying too freely on institutional and policy 'borrowing', particularly across continents, has been much questioned in recent years, both in relation to training and other policy areas (Keep 1991, Noble 1997, Ryan 1991). Differences in institutions, administrative capabilities and cultural norms all militate against successful institutional and policy transfer across countries, especially where these differences are likely to be substantial as between SSA countries and those in Latin America and Asia.

This is not to deny that important lessons for policy may be learned from international experience; but these lessons are likely to be more relevant where gleaned from practical examples drawn from countries in SSA. For this reason, the general methodology adopted in this paper is to attempt to learn from internal SSA experience rather than from afar and virtually all the country cases discussed are drawn from the region. Thus emphasis has been placed on examining particular financing mechanisms in those SSA countries where they

are in place. Scattered documentation on training finance in SSA countries, contained mainly in government and donor agency reports, has been reviewed (where available) and analyzed comparatively.

However, this documentation for SSA countries is mainly descriptive rather than analytical. Very little evaluation work has been conducted – one reason being the relatively short time periods that have ensued since these mechanisms were instituted in many countries, but a more general disinclination in the region to carry out the necessary evaluative studies is evident. Yet in examining these institutions, we need to know not only how they work but also how *well* they work. To this end, three short field studies were conducted in preparation for this paper, to South Africa, Tanzania and Zimbabwe; the findings of these visits, and lessons learned, are reported at relevant points in the development of the paper.

1.4 Coverage

The financing of training is, inherently, a topic of very wide scope. In this paper, we limit our coverage of the topic in terms of training recipients, of training providers and in the timing of training.

1.4.1 Training for Whom?

Any realistic discussion of the financing of national training systems must take account of segmentation in the employment of skilled workers and resulting differences in financing needs. In this paper, we adopt the three-way classification of training for formal sector employment, training for the informal sector and the training needs of special, targeted groups.

The vast majority of the training finance literature, reflecting the emphasis and direction of training policy, has been concerned with the needs of modern sector, notably in Government employment or in public and private enterprises. But in SSA, as in other developing regions, this formal employment sector accounts for a relatively small part of total employment and displays little growth potential. In almost all African economies, the majority of the labor force remains attached to the informal sector which includes employment in small-scale firms (micro-enterprises), non-professional self-employment and casual workers generally (ILO, 1972). It is largely within this sector that the ever-growing potential labor force might expect to be absorbed into productive employment. Finally, the focused needs of a variety of specially targeted groups have received increasing public attention in recent years. For a range of reasons, which include meeting equity, political and social objectives, Governments have usually assumed responsibility for meeting the skills needs of these groups, which include the long-term unemployed, school dropouts, the disabled, poor and underprivileged groups (including urban and rural women) and socially-excluded minorities.

1.4.2 Training by Whom?

There are many ways in which training providers may be categorized. In this paper we recognize three broad types of training mode: training in public training centers (usually, but not inevitably, under the aegis of ministries of labor), private propriety training institutions and training in companies, on-the-job. Vocational and technical education provided by the formal school system, and generally attached to ministries of education, is another component of what is usually referred to as the VET (vocational and education) system. The financing of school-based vocational education is only obliquely covered in this paper. This omission may be problematic for discussions of the working of the VET system as a whole, including such issues as alternative modes of provision and cost-effectiveness; unit costs at vocational schools are generally far in excess of those at general schools (Tsang, 1997), while vocational schooling usually fails to produce superior labor market outcomes. However, since this paper is not concerned with cost-benefit issues, the omission seems to be in order in the present context. There do not appear to be any major financing issues that relate to vocational schools, as such. The distinct financing issues of relevance to vocational education are common to secondary schooling generally, rather than to training.

1.4.3 Timing: Pre-employment, Initial and Continuing Training

Finally, we consider the timing of training, and distinguish between training received at the outset of workforce participation (pre-employment training and initial training received on-the-job) and between continuing training acquired over the working life (Jager and Buhrer, 2000).

Pre-employment training, generally acquired prior to labor market entry at formal training institutions, provides skills for future wage employment and for income generation in self-employment. This is distinguished from *initial training*: skills training received on-the-job in the early stages of employment with an employer

including, but not limited to, apprenticeship training in the formal and informal sectors.

Continuing training, acquired on–the–job or at training institutions over the working career, may focus on the up–dating of existing skills to avoid obsolescence and to enhance productivity ("refresher courses"), on skills up–grading to take on new tasks and responsibilities, or on re–training, in response to technical and structural change.

1.5 Plan of the Paper

The overall design of the paper envisages a progression from more theoretical and conceptual issues (Chapter 2 and 3) to the more applied Chapters (5–10) relating to SSA experience in training finance. Chapter 4, mapping out typical financing flows in training markets, provides a bridge between the conceptual and practical divisions of the paper.

Following this introduction, Chapter 2 takes as its point of departure the conventional pattern of training finance, as found in many SSA countries today. We discuss how these conventional financing patterns (and particularly the training provision role of government) are proving inappropriate to meet the changing needs of the economy and society. In Chapter 3, picking up on a major theme of the preceding chapter, we discuss the appropriate roles of the state in financing training and training provision. In Chapter 4, typical training finance flows are examined, from finance source to training provider. We do so for three construct training markets representing different stages on the continuum of development from conventional training finance to the type of integrated, demand–driven training markets that is regarded as constituting best–practice.

We then move on to more practical issues, illustrated by SSA country experience. Chapters 5 and 6, respectively, select for in–depth analysis the two most pervasive institutional developments in the training finance arena: national training funds and training levies. In Chapter 7 we examine alternative sources of training finance and the efficacy of measures to augment funding by finance diversification. An analysis of funding transfer mechanisms is presented in the Chapter 8, while Chapter 9 discusses mechanisms available for enhancing enterprise investments in training. Special financing issues related to training for the informal sector are discussed in Chapter 10.

While most of the paper is culled in positive terms – offering description and analysis of training finance systems and mechanisms that are at present in place in the region – the ultimate purpose of the paper is to draw lessons from current experience for policy improvement. In this spirit, each of the practical Chapters 5 through 10 concludes with a summary discussion aimed at providing some practical advice for policy, including such issues as what measures work well, advantages and weakness of policy alternatives and pitfalls to be avoided in implementation. Chapter 11 deals with the interplay between national training policy objectives and the main mechanisms for training finance. The final chapter, which serves as a concluding section to the paper as a whole, brings together the main policy messages of the paper.

2 Conventional Patterns of Financing Training

2.1 Typology of Financing Burdens

Given the classification of training provision outline in Section 1.4 (by whom? for whom? and when?), how is training financed? Who bears the cost of training? Traditionally (and leaving aside for later discussion more recent, innovative funding sources and mechanisms), the direct burden of financing training has fallen, alone or in concert, on the triad of the trainees themselves, on enterprises or on the state. A simple typology of traditional financing burdens is presented in Table 2.1.

Today, as in the past, the vast majority of employment across SSA countries is to be found within small scale, informal sector enterprises (Table 2.1, Column 1). Traditionally, initial training for the informal sector took place on–the–job, within the context of the traditional, unstructured apprenticeship, with trainees (or their families) bearing the costs of training in the form of an initial lump–sum payment and/or a low (apprentice) wage (Table 2.1, Box A1). This form of apprenticeship training, consisting largely of the handing down of initial skills for the semi–skilled and craft trades, is usually a "one–off" activity; very little continuing training takes place, subsequently. Private (for–profit) training institutions provide an additional, but very much a secondary, source of initial skills acquisition for the informal sector and small–scale businesses; enrolled students pay full–cost fees (Box A2). Church and other non–profit, voluntary training institutions may provide free or highly

subsidized initial training.

A different financing pattern is displayed for formal sector training (Table 2.1, Column II). Where initial training provides general, transferable skills, the trainee–apprentice bears the cost of training implicitly through low wages (Becker 1964). To the extent that training is not freely transferable because, for example, some skills are of specific use to the firm or training markets are not freely competitive, the enterprise assumes some of the burden of financing initial training. Similar considerations apply to continuing training provided by the enterprise, with cost sharing between the worker and the firm reflecting the extent of skills transferability (Box A2). Training in pre–employment skills, acquired at private markets at proprietary training institutions, is paid for by students; continuing training at these private training institutions may be financed in combination by the enterprise and the worker, or by one of the parties individually, again depending largely on potential skills transferability. To a lesser extent, subsidized initial training may be provided at voluntary training institutions.

All of the above forms of training take place within private markets and are essentially demand–driven, focused on meeting market demands for skills. Yet these traditional private markets have proved to be too limited to meet the broader skill needs associated with economic development and growth. Thus in nearly all developing countries public training systems have been established, in parallel. The State has emerged as a major player in the training markets of most countries. It is a leading supplier of structured, pre–employment training provided in public training centers (as well as in vocational schools), to the extent that it frequently dominates the market for training. Yet the State is dominant not only as a major provider of training (mainly for the formal sector but also for informal sector employment). It is also a major financier of pre–employment training (Table 1.1, Row C); courses at public training sectors are either provided free or at purely nominal fees. Continuing training at public training centers is also usually highly subsidized, though enterprises may pay up to full costs for sponsored training or specialized courses at public training centers.

Table 2.1
Conventional Patterns of Financing Training in SSA

Training Provider	Employment Sector		
	1 Informal Sector	2 Formal Sector	3 Special Groups
A Employers:			
Initial training (on–the–job) – Apprenticeship	Trainee financed	Trainee/Enterprise financed	---
Continuing training	---	Enterprise/Worker financed	---
B Private Institutions:			
Pre–employment training	Student financed	Student financed	---
Continuing training	---	Enterprise/Worker financed	---
C Public:			
Pre–employment training	State financed	State financed	State financed
Continuing training	---	State/Enterprise financed	State financed

Note

--- Not applicable or of limited importance

The rationale for State intervention in training markets, in both the provision and the financing of training, has been much debated, particularly in relation to training for the formal sector. The strongest case for Government provision of training can be made when private institutional training capacity is weak, inefficient or under–developed. However, the case for the blanket supply of subsidized State–provided training – without payment or at nominal fees only – is less readily made, even though this is the pattern in very many countries round the world. We return to this issue, with a fuller discussion, in Chapter 3.

The arguments are somewhat reversed for the provision of training for special target groups at government training centers (Box C3). Governments have increasingly assumed special responsibility for the improvement in the life-chances of particular socially disadvantaged groups in the population. Seeing skills acquisition as a valuable tool for achieving these aims, many Governments have responded by providing free training courses, often specially designed, for these at-risk groups. Indeed, a strong case can be made, on social grounds, for training subsidy for these groups, met out of public funds; however, Government training *delivery* is less clearly justified, particularly where alternative private training provision is in place or could be developed.

2.2 Shortcomings of Conventional Training Financing

The simple financing framework outlined in Table 2.1, still current in many developing countries today, has become inadequate to meet society's skill development needs. A number of emerging trends, which include but are not confined to those listed below, have rendered this framework increasingly outmoded.

* An increasing problem in many training systems is a tendency to market failure, with firms under-training, particularly in transferable skills. This is the case both in terms of the amount of training provided and its quality. The presence of labor market distortions, such as overly narrow wage differentials, leading to weak incentives for workers to acquire skills, is prevalent in many developing economies. The risk that workers trained in both general and specific skills may move to other firms, as well as the strong incentives for firms to poach trained workers rather than invest in training their own workforces, may lead to training under-provision by firms and to chronic shortages of well-trained, skilled workers in the formal sector. This in turn stunts productivity growth, competitiveness and industrial development. Governments may intervene with corrective measures, often a combination of financial incentives and compulsion, to increase the quantity and quality of enterprise-provided training.

* Ongoing technological change, structural adjustment policies, new and changing patterns of trade and competition, and globalization have combined in many countries to create the need for a much more flexible and responsive training system for the modern sector, than has been manifest in more protected regimes in the past. These ensuing changes lead to continuing, and more substantial, changes in skills demands in the labor market over time; but the more changeable is the market demand for skills, the more flexible must be the supply response from the training system. Training systems for the formal sector are failing to respond to these emerging external challenges, essentially, because they are too static in nature. They may be seen as static in a number of senses. Firstly, training horizons are limited. Pre-employment and initial training for the formal sector have concentrated too much on one-time learning for immediate employment; but the dynamics of labor markets and changing skill needs over the working life require a more forward looking approach, emphasizing future trainability in addition to the skill needs of immediate employment. Similarly, enterprises are largely reactive (focusing more on immediate needs) rather than being proactive in relation to investing in continuing training. Secondly, the institutional environment within which public training systems operate, with accountability to a government ministry, often results in training provision that is largely isolated from market forces, is subject to slowly-changing, centralized curriculum decisions and is circumscribed by limited institutional autonomy. Such public training systems, widely referred to as supply-driven, are unlikely to be responsive to the changing skill needs of a growing, competitive economy. These shortcomings may be overcome by the adoption of carefully selected training finance policies, with an appropriate blend of incentives, of compulsion and of mechanisms to change the competitiveness of the training environment.

* Fiscal restraint is a central feature of structural adjustment policies, introduced in many developing economies. Increasingly, limited public sector budgets have seriously constrained the ability of governments to provide adequate and stable funding to the public training sector. In other economies, parsimonious public budgets result from the heavy reliance on revenues from indirect taxes, such as domestic excise taxes falling on a narrow range of commodities and taxes on internationally traded goods. Broadening the tax base to include the direct taxation of personal income, as in industrial economies, may not be feasible in many developing countries: not only is formal sector employment relatively small but there are difficulties in taxing the urban sector and the large and widely scattered rural population. Pressures on the central budget and the lack of constant and adequate funding for public

sector training has led to the identification and tapping of alternative sources of funding, including a greater degree of cost sharing amongst the beneficiaries of training programs.

* In many developing countries, demographic change and high population growth rates have resulted in very substantial increases in the numbers of labor force entrants. For Africa, it is estimated that labor force entries will continue to outnumber departures by a factor of three (Wander, 1987). The result has been high unemployment, underemployment and low wages, especially for a country's youth. Since in many SSA countries, the modern employment sector remains small and stagnant with little potential for expansion over the medium to long term, an expanding urban informal sector is being seen increasingly as a major source of manpower absorption and employment growth. These trends will require a redirection of training supply towards meeting more directly the particular needs of informal sector development, in terms of job skills provision and entrepreneurial skills.

* There is currently an increasing social awareness (and conscience) concerning the low current status and skill needs of special groups, such as the poor, ethnic minorities and women. In parallel, there is a wider acceptance that the government has an obligation to assist in this field, through financing and perhaps skills provision; yet these groups are likely to succeed in securing employment only through post-training entry to the informal sector. These developments are likely to be heavily constrained by lack of available government funding because they are coincident with increasingly limited public budgets and greater inter-sectoral competition for funding allocations. This indicates, perhaps, an appropriate role for donor intervention.

2.3 Changing Roles for the State, Enterprises and Individuals

In order to meet these challenges, training systems in many countries, and the ways in which they are financed, will need to adapt to the new realities. This, in turn, will require a critical reexamination of the current role of the state, enterprises and individuals in training markets and how these roles will need to change. Directions of change will include the development of private training markets, increased competition between public and private training providers, declining roles for the state in the financing and provision of training, a greater diversification of funding sources for skills development (including enhanced cost recovery, cost sharing and training levies), the encouragement of more and higher quality enterprise training and meeting the needs of the informal sector. In subsequent chapters of this paper, these themes will be developed and applied to the SSA context. That discussion, however, is underpinned by the two more conceptually-based chapters that follow.

3 The Role of the State in Financing Training

Funding mechanisms are aimed, in part, at augmenting the supply of training resources. We have noted that in conventional training markets it is the state, rather than the direct beneficiaries, that bears the major burden in the financing of training for the formal sector, particularly pre-employment training. Thus reaching out to new sources of training finance would entail usually a lightening of the finance burden that falls on the government (either in the funding of the current training system or its expansion). Indeed, this is often the motivation for diversifying sources of finance through cost shifting to other actors. Cost shifting may be in order also in situations where existing government funding of training is thought, in some sense, to be excessive. But are existing levels of state funding of training excessively high? Thus prior to any consideration of measures that may be taken to reduce this financing burden (in relative or absolute terms), it is fitting to look more closely at those factors that may justify government financing of training. Against this back-cloth, the issue of defining the appropriate role for governmental intervention in financial training markets may be more readily assessed.

Discussion of the appropriate role and level of government intervention in the financing of training is frequently confounded by the double role assumed by government in many training markets – it both acts as a training provider and also finances training. The clearest example is afforded by government provision of pre-employment training without charge, at public training centers. But these dual functions are not inextricably connected. The state could finance similar training at private training institutions or it could charge full-cost fees for the courses it provides.

3.1 Rationale for Government Intervention

In this chapter we examine seven major arguments often adduced, differentially, to justify a government role in financing and/or provision of training. These are summarized in Table 3.1, which lays out in schematic form the conclusions of this chapter regarding the roles cast for government in financing and delivery of training; these are conditioned largely by the efficiency with which training markets function. The table builds on an earlier formulation (Ziderman 1990), which formed a central thrust of the approach to these issues presented in the World Bank policy paper on vocational education and training (World Bank 1991) ⁴.

3.1.1 External Benefits

Of the arguments for a public role in training, the government response is clearest in the case of market failures in the form of 'externalities'. Positive externalities exist where the benefits of training that accrue to society exceed the private benefits realized by trainees and firms. Thus from a societal perspective, the decisions of trainees and firms will lead to a shortfall of spending on training. Thus, for example, the shortages of a particular skill might inhibit the development of a new industry that is strategic for growth. Wages offered for these, potentially bottleneck, skills may fail to reflect the future social benefits that the employment of these skilled workers will provide, with the result that shortages of the new skill impedes the development of the strategic new industry. This version of market failure justifies training subsidies but not necessarily provision (Table 3.1). The cost of subsidizing training may be met out of general taxation legitimately on the grounds that society as a whole benefits (via its externality effects) from the extra skills thus generated.

This type of externality argument, often advanced to justify general education subsidies, is generally less strong for training, which may be more narrowly focused on providing skills relevant to particular occupations. Apart from the potential bottleneck type of argument advanced above, the more narrowly conceived is the training, the fewer are the wider societal benefits it will provide and the weaker is the case for public subsidy. A major problem with this traditional externality argument is ascertaining what is the appropriate size of the justified subsidy, given the elusive nature of many of these externality benefits and the notorious difficulties associated with their measurement. The danger of costly over subsidization of training is ever present.

Table 3.1
Policy Options for Public Intervention in Training Markets

Reason for intervention	Policy Options			
	State subsidy of training	State provision of training	Complementary policies	
Externalities	P	N	–	None
Property rights	A	N	P	Levy–grant schemes
Market imperfections	A	N	P	Deal with sources of market imperfections*
Inadequate enterprise training	A	N	P	Build up enterprise training capacity Levy–grant schemes
Weak private training provision	N	A/P	P	Build up private institutional training capacity
Parity	A	N	P	Reduce subsidies to trainees' peer groups, together with introduction of selective scholarships
Disadvantaged groups	P	N	P	Targeted training subsidies Employment creation Income redistribution

Notes

- P = Preferred policy approach**
A = Acceptable (second–best) approach

N = Policy not justified
*** = Policies may not be feasible**

3.1.2 Property Rights

The presence of externalities constitutes the classic form of market failure, justifying government financial intervention in such markets. We now turn to a rather different form of market failure that is particularly relevant to training markets. Unlike company investment in capital assets such as plant and machinery, firms do not have property rights over the human capital created by training, which is vested in their workers. This may give rise to the 'poaching problem' – the tendency for firms to recruit (or poach) from other firms, workers trained in transferable skills, rather than train their own employees. Poaching imposes costs on firms that train because of the greater wastage of newly trained workers to poaching firms and the loss of any training costs incurred. Training firms will react by cutting down on their training efforts or by offering training that tends to be narrow and not readily transferable, i.e. that is unlikely to yield externalities or carry a high societal return (Katz and Ziderman 1990). The result is a general under-provision of trained workers.

The preferred policy is the introduction of levy-grant schemes, based on payroll levies, and thus not requiring government finance (discussed more fully in Chapter 9). The rationale of levy-grant schemes is the cross-subsidization of training firms, financed by the levy paid by non-training firms (potential poachers). Corrective government subsidies, offering training incentives to firms, may be acceptable (as a 'second-best' solution), particularly where externality benefits might accrue; but there is no justification for government training provision.

3.1.3 Market Imperfections

If training markets work imperfectly, under-investment in training may result. A major source of training market imperfections stems from unintended side-effects of economic and social policies that distort incentives for individuals and enterprises to invest in training. Government wage policies resulting in compression of wage differentials for equity reasons, provide an example of these policies. This compression reduces private incentives to acquire skills. The preferred solution is for the government to address the policy source of the market imperfection, but this may not be desirable or politically feasible. In that case, government intervention in the financing of training to offset the imperfection, may be justified; the subsidies could take the form of training grants to individuals or subsidizing enterprise training. The aim of the training subsidy would be to restore a positive balance between the private benefits and costs of training, so that incentives for private investments in skills acquisition remain sufficiently high.

3.1.4 Inadequate Enterprise Training

Enterprises may be reluctant to discharge their training role adequately. Non profit-maximizing behavior by firms may lead them to under-train. Managerial lethargy, a noncompetitive production environment and a lack of company foresight are among the reasons that companies may fail to organize structured in-service training, particularly apprenticeship training. This lacunae does not make out a case for government training provision. While subsidies may be useful as an incentive to companies to build up training capacity (including the subsidy of apprenticeship wages), more proactive approaches are preferred, particularly over the longer term. These include both the offering to firms of training advisory services and technical assistance by government (or by a national training fund) to improve training capacities, and also the strong incentives provided by levy-grant schemes.

3.1.5 Weak Private Training Provision

But in countries where the modern sector is underdeveloped and the size of enterprise small, there may be an insufficient enterprise base to provide the capacity for structured, low-cost training. This would open the way for the growth of private, specialized training institutions; yet such initiatives may not be forthcoming, particularly in lower-income countries, due to a lack of know-how, capital shortages and constraining regulatory policies of government. Here, the public sector may perform a critical role in meeting skill needs. But government provision is seen best in terms of performing a transitional role, as government encourages and facilitates the developing of private training capacity; this would then complement and provide a more competitive framework for training provision by the public sector.

3.1.6 Parity

The final two arguments are concerned with social issues. The first, relates to the heavy subsidies given to secondary schooling and tertiary education in many countries. These are a source of social inequity, particularly when the beneficiaries come from privileged backgrounds. Here the parity argument for extending subsidies to individuals undergoing training is quite strong (in the case where trainee peer group subsidies cannot be reduced substantially), particularly where pre–employment training is directed more towards less privileged individuals.

3.1.7 Disadvantaged Groups

The second social argument concerns the training needs of various disadvantaged groups in society, for whom training is regarded as an important tool for improving their incomes and employability. As we noted in Section 2.1, there exists a broad consensus, matched by practice in many countries, that it is the task of government to ensure that these needs are met. Where in place, these special programs are financed out of the public purse through the provision of courses at public training institutions. While public finance of these training programs is justified, public delivery is less so – particularly where alternative private training provision is available or could be developed.

3.2 Designing Appropriate Policy Interventions

Conditions for government intervention in training markets are present in virtually all countries. However, because the economic environments, which shape the incentives for employers and individuals to invest in training, differ across countries and are subject to change, there can be no single prescription for policy on state intervention in training markets. Rather, the role of governments in the provision and financing of training has to be based on local conditions and informed by careful economic analysis. The policy matrix provided in Table 3.1 is best seen as a checklist for probing the justification for training market intervention policies, in a given country situation.

What conclusions for policy in SSA countries may be drawn from this discussion? We note three central conclusions for policy.

The first is that the appropriate role of government in training markets is to let private training markets work where they function well and, where they do not, to engage the public sector. This definition of the government role in training finance and provision requires a country to determine its own needs for public sector training intervention. It will need to examine the performance of its markets, the capacity of the private sector to deliver training and its own preferences with regard to social policies and equity. On this basis, there is likely to remain a continuing role for the state in many countries in the delivery and, particularly, in the financing of training.

The second is that there is probably much more public *provision* of training than is required by economic rationale alone. But this may not be sub–optimal if public training is efficient, effective and market–responsive; unfortunately, frequently, this not the case. An important task of funding disbursement policies, as discussed in Chapter 8, is to provide an appropriate mix of regulation and incentives to ensure public training can hold its own in an environment of competitive training markets.

And third, it seems to be the case that there is far more public *financing* of training than is really justified by the economic arguments adduced above. Given the increasing pressures on government budgets, this conclusion provides an opening for funding diversification – a major theme of this paper.

4 Finance Flows: Three Scenarios

We have noted that much of the available literature on training finance mechanisms does not do a very good job in contextualising these mechanisms. In particular, insufficient attention is given to showing how various mechanisms inter–react and how they relate to the existing training financing system as a whole, in terms of their purpose and how they contribute to the achievement of defined objectives. The purpose of this chapter is to place the subsequent discussion of particular financing mechanisms within a broader framework of the overall system of training finance.

We discuss three broad scenarios, corresponding to progressively higher levels of maturation of training finance systems. The first relates to traditional training finance flows in conventional training markets, as discussed in the previous chapter: a bureaucratic, government financed and controlled public sector, providing

pre–employment training coexists with private training markets for informal and enterprise training. We then move on to training markets where the state continues to exert a powerful influence on training for the formal sector, but of a different kind. Now the state acquires a stronger role in regulating the financing system through ear–marked training levies (particularly in relation to enterprise–provided training) but where also parsimony in state financing of public training institutions leads to the increased financial diversification of public training. Thirdly, we look at modern, integrated financing systems, displaying strong moves towards competitive, demand–driven training markets. It should be emphasized that these scenarios are presented as synthetic constructs to guide our understanding of policy development, rather than as descriptions of actual, delineated stages in the evolution of training systems. Not every country will fall neatly into one of the three categories; some country situations will span across categories.

4.1 Conventional Training Markets

As a point of departure, we consider major finance flows in conventional training markets, as reflected in the discussion in Section 2.1 (and Table 2.1). A schematic overview is presented in Chart 4.1. Institutions that provide training are indicated by the white boxes. As we have noted, training may be provided through private training markets either by firms or in proprietary training institutions; it may also be provided within the public sector at public training institutions. However, the training market is fragmented into two distinctly differing sectors – private and public.

The major training providers in the private sector are enterprises and proprietary training institutions. The private training sector is market–driven, non–subsidized and (usually) competitive. Firms (in both the informal and formal employment sectors) provide training to trainees/workers in their employ; payment is made by the employee/trainee through initial lump–sum fee or implicitly in the form of low, below–productivity wage levels. Individuals enroll in pre–employment courses, at full fees, at private training institutions; training fees for continuing training may be borne partially by formal sector employers.

In contrast public sector training institutions are, predominantly, financed from Government budgetary allocations. Where they are current, student fees are set at purely nominal levels and often accrue to the government rather than remaining with institutions. Firms may enroll their workers for continuing training courses, provided at full cost but more usually at subsidized fee levels. Because budget allocations to public training providers are usually unrelated to objective, outcome measures – such as success in placing trainees in productive employment – there is little incentive for training providers to align training courses offered, with the needs of the labor market. Linkages between public training centers and formal sector employers remain poor; training provision is dominantly supply–driven. Moreover, training centers do not develop training programs focusing on the particular needs of informal sector employment nor do they cater well for the special needs of minority and disadvantaged groups.

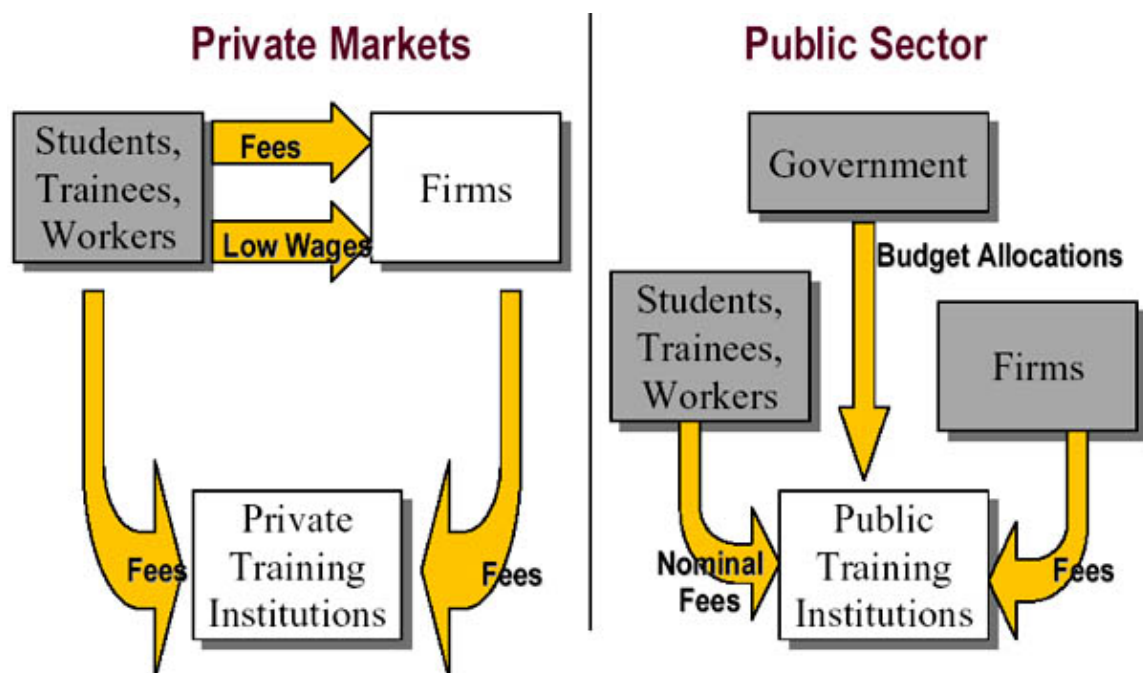


Chart 4.1 Finance Flows: Traditional Fragmented Training Markets

There are many SSA examples of this scenario, including Ethiopia, Mozambique and Zambia. These financing markets display many of the traditional shortcomings, discussed above, that training finance (and more general) reforms aim at correcting. Zambia is currently engaged in a process of training policy and finance reform; this will move it strongly in the direction of the second scenario, which we now discuss.

4.2 Training Markets with State Intervention

While such conventional training markets remain in place in many African countries, in others a strong trend away from these traditional forms of training finance and provision is in evidence. The driving force behind these moves has been the increased intervention of the state in training markets; paradoxically, this process has involved a *retreat* by the state in the financing of training. Increasing pressures on government budgets in general, and on public training budgets in particular, has led to a search for additional or alternative sources of funding for training. In addition to the need to tap non-government sources of funding, governments have intervened more strongly in training markets in order to counter shortcomings of conventional private training markets and notably the tendency for enterprises to under-train.

The process of funding diversification has taken a number of forms. The most important by far has been increased sharing of the cost burden of public sector training by other beneficiaries of training, notably firms and workers. Chart 4.2 shows the major financing flows.

In many countries round the world, special taxes earmarked for the support of training have been adopted – indicated by (1) in the Chart. The predominant format has been a percentage levy on company payrolls. Payroll levies offer a means of mobilizing funds for training that are otherwise inaccessible to the public sector. First introduced in Brazil in the 1940s, they have emerged as an important alternative to government budgetary allocations to the public training sector in many developing countries, as well as in a number of industrialized economies. In these cases, cost-sharing is the rationale underlying the imposition of payroll levies which generate revenues for the support of public training: firms are the partial, though indirect, beneficiaries of publicly-provided training, in terms of a better-trained workforce, enhanced productivity levels and greater profits, and should share in its costs.

Increased cost sharing may be effected also through the raising of course fees at public training institutions. We have noted that such training is traditionally provided free, or at purely nominal fee levels, in many developing countries. But trainees are the major and direct beneficiaries of these training programs, in terms of improved employability, greater productivity and higher incomes, whether from wage- or self-employment. This indicates that greater cost recovery, through the imposition of more realistic (albeit still subsidized) trainee fees – item (2) in Chart 4.2 – is both justified and feasible. However, the raising of fee levels for public training may need to be accompanied by the availability of selective scholarships for the poor and disadvantaged.

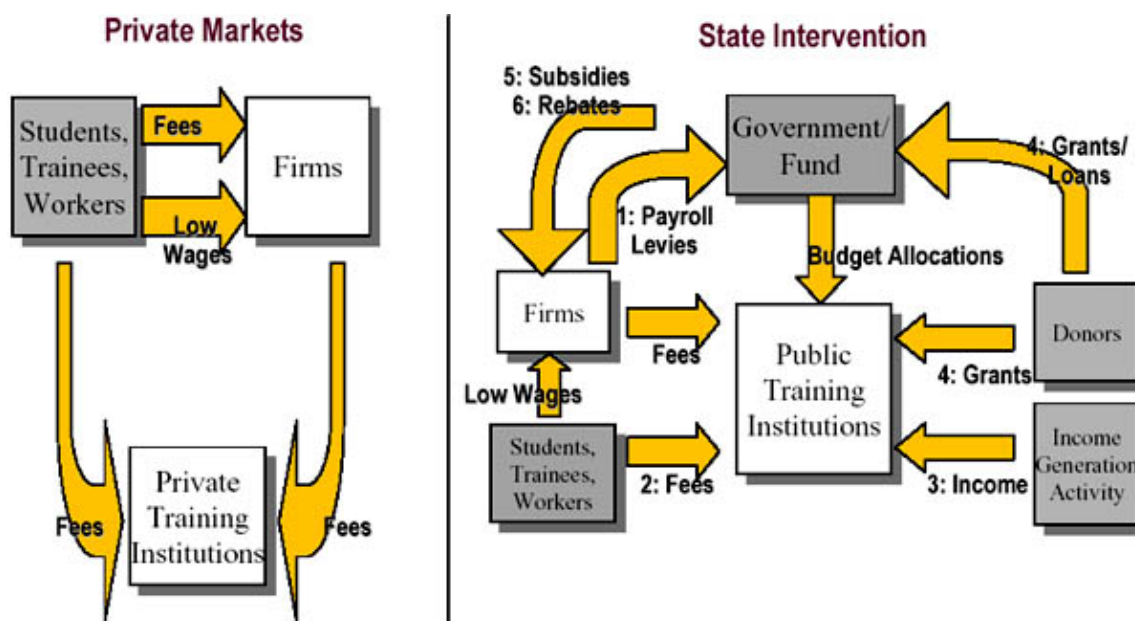


Chart 4.2 Training Markets with Strong: Finance Flows State Intervention

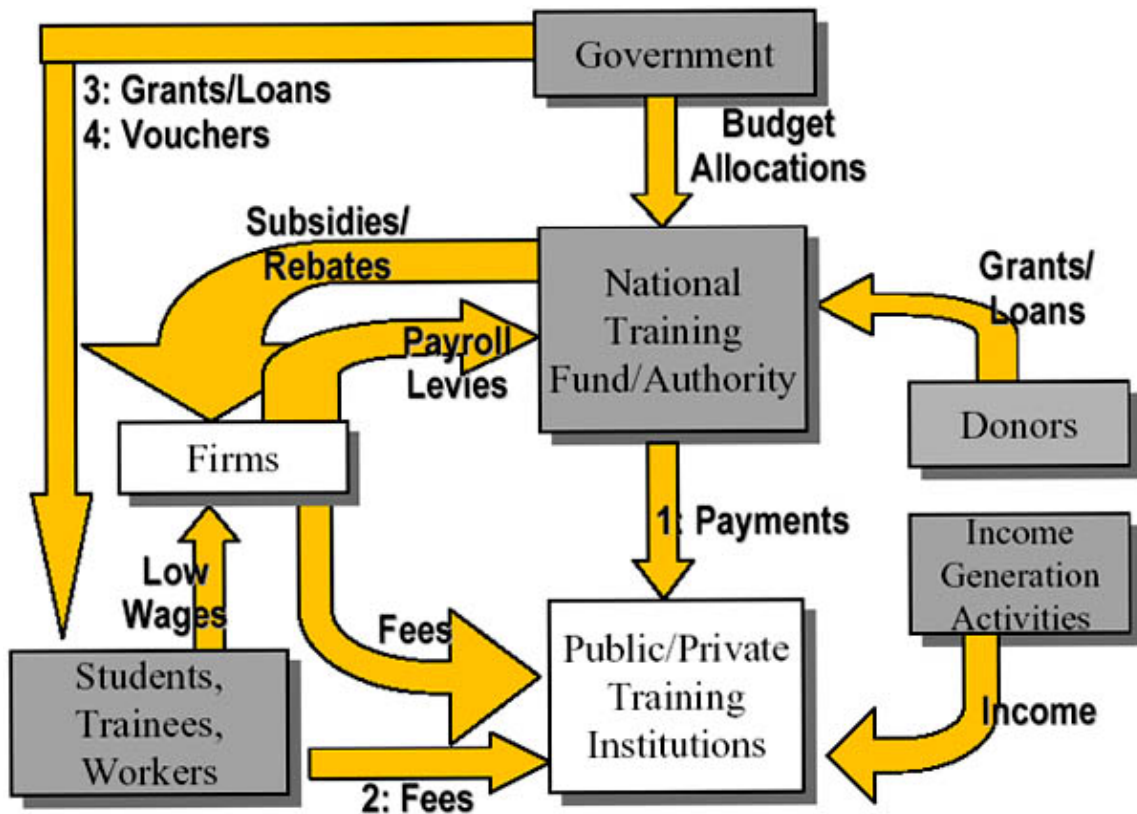


Chart 4.3 Driven – Integrated, Demand: Finance Flows Training Markets

An additional, though limited, source of funding diversification for public sector training is income generation by public training institutions – (3) in the Chart. Examples are the generation of income from production within the training context and the hiring out of underutilized facilities. Finally governments may turn to donor institutions to provide funding, either to the government or directly to individual training institutions (4); in some country settings, donor funding constitutes a very important finance source for public sector training institutions.

A second major reason for government intervention in conventional training markets is a corrective one: to encourage formal sector enterprises to provide more and better training. Governments subsidize enterprise training, either directly from central government budget appropriations or, less usually, from specially designated training funds, also financed (fully or in part) by government – (5) in Chart 4.2. But tight public budgets may limit the government's ability to subsidize enterprise training from public funds. Levy-grant schemes, based on payroll taxes, have provided governments in many developing countries with an alternative mechanism for promoting company training. Unlike the "revenue-generating" rationale for payroll levies discussed above – where the revenues from training levies are earmarked to finance public sector training institutions – levy-grant schemes are directed towards training provided by enterprises. While many variants are found in terms of actual practice, the common feature of levy-grant schemes is the provision of incentives for firms to provide more and better training. Payroll levies are often linked to reimbursement mechanisms, whereby firms receive payments related to the amount of designated forms of training they provide – (6) in Chart 4.2. Payroll tax revenues are distributed as rebates, usually up to a specified percentage of the tax paid, to firms that set up or broaden programs of in-service training.

One outcome of the introduction and spread of earmarked training levies has been the development of a relatively new type of financing mechanism: the national training fund (Fund). These Funds usually constitute both the depository of collected training levies and also the mechanism for their distribution. Government budgetary allocations may supplement levy income to the Fund, or represent its major income source; donor support is important in some cases. The intention is to provide a sheltered funding source for national training development, including the financing of public sector training, the provision of incentives for enterprise training and meeting the skill needs of special groups. Training funds usually operate outside normal government budgetary channels; thus they are more readily accessed and may be utilized more flexibly than would be the case normally with direct government financed training programs. However, operating as they do under varying degrees of autonomy from government control, a Fund's freedom of manoeuvre may be constrained. Thus in cases where the degree of independence from Ministry of Labor and Treasury control is limited, the Funds may often emerge as conservative, reactive bodies, rather than adopting a proactive, independent

stance in fund policy and management.

Overall, this stage may be seen as one that strengthens the market orientation of the training system. Government intervention in training markets is emphasized rather than direct government financing and control. There is a strong move towards diversification of training finance. Drake and Germes (1994) notes that an element in this shift "is to change the means of raising funds from general taxation, by definition unrelated to training or to structural shifts within the economy, towards dedicated taxation like payroll taxes."

The training finance system currently in place in Zimbabwe may be seen as an example of this scenario; it illustrates certain weaknesses associated with the financing systems typical of this scenario. Recent training reform legislation in Tanzania is moving that country's training financing system towards scenario 3. Both cases will be discussed subsequently.

4.3 Integrated, Demand-Driven Training Markets

In many SSA countries, the training finance mechanisms that are presently in place conform broadly to the schema set out in Chart 4.2. But these training finance systems suffer from two major shortcomings. Firstly, public training provision remains essentially supply-driven. It is not subject to the discipline of competition with other training providers; nor are guidance mechanisms in place to match the skills supplied by public training institutions with the skill needs of the market. Secondly, and related to this, while the training finance system is more integrated than that illustrated in Chart 4.1 (with formal sector enterprise-based training, as well as public sector training, now subject jointly to policies of state intervention) much fragmentation remains. In particular, private training institutions do not operate within the same financing framework as public sector training providers. Corrective mechanisms have been introduced in a number of countries; these are shown in Chart 4.3, which relates to training finance flows in more integrated, demand-driven training markets.

In many countries national training agencies or authorities (NTAs) form the linchpin of the financing system. NTAs may be attached, with varying degrees of autonomy, to a government department (usually the labor ministry), but they are likely to operate more effectively as largely autonomous bodies forming a buffer between government and the training system. They are usually run by boards representing the training system's major stakeholders. While most NTAs receive general government funding, a large number are financed solely or in addition, by payroll levies. NTAs are much broader in scope than training funds; they are usually empowered with a wide range of national training responsibilities. In addition to managing the system of enterprise training subsidies and, where levy-grant systems are in place, levy reimbursements, they may be charged with responsibilities for developing national training policies and standards, planning the national training system, accreditation of institutions and generating and disseminating relevant labor market information.

NTAs may be better placed than environmentally-constrained government departments to operate payment mechanisms for training institutions in ways which promote efficiency and competitiveness in training markets – (1) in Chart 4.3. Formula funding of public training institutions (such as output-related funding) provides one example of such measures. Contracted training, particularly to meet the needs of disadvantaged groups, is another. Based on competitive tender that is open to public and private training institutions, contracted training can, through the bidding process, both integrate training markets and pressure public training institutions to be more efficient and to operate at lower cost. In line with this approach, donor agencies would fund the NTA only, not individual training institutions.

In parallel, other moves towards more open, competitive markets may be taken. Fees at public training institutions may be raised closer towards competitive levels (2), facilitated by the availability of selective scholarships for the poor or student/trainee loans (3). The introduction of a supportive policy framework to facilitate the development and growth of private training provision is complementary to this approach. Vouchers may be made available to potential trainees to purchase training in the open market, with public and private training providers competing for trainee enrollments (4).

Recent training finance reforms in South Africa, currently being implemented, provide an example of a system moving strongly in the direction of scenario three though, notably, not in all aspects; the South African case will be discussed in detail at various points in the paper.

4.4 The Pace of Reform

These scenarios have been presented in terms of successive stages in an evolutionary process leading to the third scenario. Essentially, these stages can be seen as representing positions on a spectrum ranging from government finance, provision and control to integrated and free (or simulated) training markets.⁵ We have noted also a consensus in the survey literature on training finance systems that argues strongly in favor of training financing systems displaying many of the characteristics of scenario 3. This should not be seen as suggesting that all SSA countries with "lower-stage" training finance systems should embark on drastic reforms leading to training finance systems approximating to the third scenario. As Drake and Germe (1994) remind us: "... most financing innovations are regime modifications". Each country will need to advance at a pace that is consistent with its present state of economic and social development and which takes account of implementation constraints imposed by limitations in existing institutional and organizational capacity. This indeed, is how 'best practice' should be understood – as a relative rather than absolute concept, defined in terms of practices best suited to a country's stage of economic and institutional development.

Thus some countries would need to advance more quickly on some aspects of financial reform than on others. For example, comprehensive plans for training finance reform in Zambia, as outlined in a government strategy paper (Ministry of Science, Technology and Vocational Training, Zambia 1997) and which were in line with reform trends in other countries, included the imposition of a payroll levy to finance a national training fund. These plans have now been scaled down following second thoughts on what is presently feasible and in the light of implementation capabilities; in particular levy financing of the training fund has been postponed to a later stage. In Madagascar, also, implementation of a payroll levy was held back, while moving ahead with other funding reforms. Experience in Togo is instructive. With donor support, plans were developed to restructure the training system to become more demand-driven and responsive to the needs of the production sector. These proved to be overly ambitious given the available capacity of key institutions and the motivation of private sector actors, whose active participation was an essential ingredient for effective restructuring.

5 The Development of National Training Funds

5.1 Origins and Objectives

Training funds are a central element in the training finance system in many countries round the world. They are in place in the majority of SSA countries; their establishment is on the policy agenda in a number of others. Training funds constitute an institutional framework for the allocation of funding to training providers; they are usually concerned also with enhancing the supply, quality and relevance of training provision. Yet, not all training funds share the same objectives, have the same coverage or operate in the same way. For a clearer understanding of the workings of training funds it is necessary to examine them from a number of differing viewpoints: particularly in terms of their defined tasks, organizational structure and sources of income and disbursements.

The origins of training funds may be traced back to the development of earmarked training levies. The earliest forms of training levies – assessed on the total payroll of enterprises were developed in a number of Latin American countries, as an integral part of the working of employer-based national training boards. Levy income was designated mainly to fund public training institutions run by the training boards. The process was usually concerned with both the collection and management of levy funding; a protected depository was required for the dedicated proceeds of the levy: hence the growth of special training funds.

Training funds have since been developed in many countries. But the line of development has not been uniform, depending on a range of factors such as differing historical origins, policy objectives and institutional framework. Some training funds are centrally concerned with funding disbursement to training providers – both training institutions and enterprises; others constitute the disbursement arm of national training authorities/boards (to be considered later in this chapter), which are charged with broader national responsibilities, such as training provision, institutional accreditation, national training policy. Some act as autonomous bodies, usually under the aegis of a (usually tripartite) advisory board; for others, freedom of independent action is constrained by ministerial control – often a ministry of labor. Most training funds receive their income from training levies, alone or in concert with funding from other sources, mainly government budgets or donor payments; in other cases, no training levies are in place and government and donors remain the major income source. Some funds are empowered to provide funding to a wide range of training providers and forms of training; others are charged with responsibilities for a more limited part of the training spectrum.

Thus the objectives – and therefore the range of activities – of training funds vary widely from country case to case. "The characteristics of individual training agencies (funds) vary so greatly that it is difficult to generalize about them (Herschbach 1990). Thus the concept of 'best practice' in relation to training funds is somewhat nebulous given this heterogeneity in objectives and in practice. Nevertheless, in the final section of this chapter, and derived from the ensuing discussion (which includes a consideration of cases in SSA where practice falls short of desired standards), we do attempt to formulate a scenario that might be regarded as representing the growing consensus on the appropriate role of training funds and good practice. Before offering prescription (in Section 5.9), we begin our discussion in positive terms.⁶

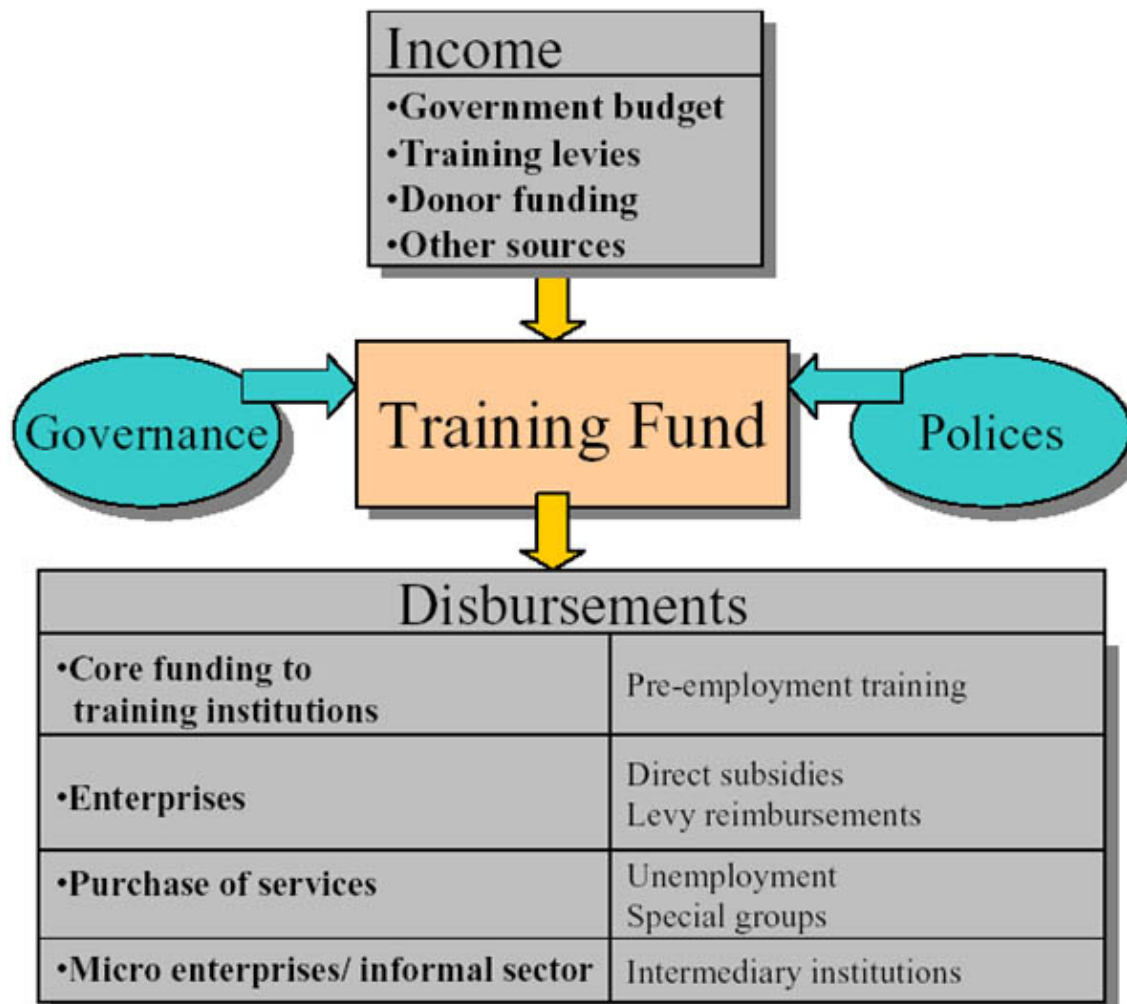


Chart 5.1 Framework of Activities: National Training Funds

5.2 Range of Activities

A national training fund may be seen as an institutional framework for unifying and augmenting public sources of funding for training and for allocating funds in line with national policies and priorities. Chart 5.1 indicates this range of activities. While in older established training funds, training levies were the dominant (usually only) income source, the chart emphasizes the variety of available income sources: government budgetary allocations, donor funding and income generated by the fund itself. Indeed, in some cases, the training fund derives no income from training levies; either levies have not been instituted or, where in place, levy proceeds are regarded, in practice, as general tax revenues and not passed on to the fund.

On the disbursements side, we note that the range of institutions and training forms eligible for funding support also may vary markedly from case to case. Earlier training funds based on payroll levies were largely single purpose – aimed at financing public sector pre-employment training (revenue generating schemes) or at enhancing the amount and quality of enterprise training investment (levy-grant schemes). There were some examples of mixed objectives – a case in point is the Nigerian Industrial Training Fund, at first only a levy-grant scheme, subsequently also provided pre-employment training at its vocational training centers. But in all these cases, levy income was not only committed to pre-designated disbursement targets; there was also a large degree of consonance between those who financed the levy and those receiving the

benefits of the training – a theme we develop more fully in the next chapter.

With the broadening of training funds both in terms of income sources and the allocation of disbursements, this link has been considerably weakened. Training funds are now increasingly regarded as a general funding pool, distributed across various recipient destinations according to established priorities and policies; this results frequently in a considerable degree of cross-subsidization of training. Even in the new funding arrangements in South Africa, where business opposition to the imposition of a national payroll levy had been strong, a fifth of payroll levy income is being assigned to a central fund (supplemented by government allocations) to finance largely non enterprise-related training.

5.3 Income Sources

We turn first to income sources. We have noted the strong connection traditionally between payroll levy systems and the development of training funds. At the present time, however, sources of income for training funds are notable for their diversity. The major income source of most training funds remains training levies, usually but not invariably, levied on enterprise payrolls; however, government budgetary appropriations and donor funding are becoming increasingly prominent and some training funds may generate additional income from other activities. Where training levies are in place, they may be levied on a uniform basis (e.g. a standard percentage of enterprise payrolls) or they may vary (say across sectors). Once collected, levy proceeds are usually administered through a central fund; however, other arrangements may be preferred, such as the use of separate sectoral-based funds (see Section 5.6).

5.3.1 Country Examples

Table 5.1, relating to eight different income source combinations in selected SSA countries, illustrates some of this diversity.

The *Zimbabwe* Manpower Development Fund (ZIMDEF), at least formally, is typical of classic funding arrangements: a uniform, centrally administered payroll levy being the sole income source. More recently (as discussed below) ZIMDEF has benefited from considerable investment income derived from levy surpluses and real estate investments, an aberration from accepted practice.

The former Industrial Training Fund in *Malawi* (currently being replaced by a broader-based funding scheme) financed the national apprenticeship scheme through reimbursement of apprenticeship wages and grants to technical colleges. Training levies, again, were the sole funding source; they were in the form of a differentiated head tax on skilled workers, by skills- category rather than a payroll levy. In *Cote d'Ivoire* and in *Tanzania* levy income is supplemented by donor contributions and, in *Cote d'Ivoire*, by government funding. Formally, the National Training Fund in *Togo* is also financed by a payroll levy, the government and donors; in practice the proceeds of the levy remains with the Treasury and are not transferred to the Fund.

The new funding system being established in *South Africa* is financed by a uniform one percent payroll levy. Eighty percent of proceeds are allocated to new sectoral training bodies (SETAs) for disbursement within their sectors. In *Kenya*, the Industrial Training Fund is funded by eleven separate sector-based training levies; separate sectoral accounts are kept with no cross-subsidization across sectors. In *Madagascar* the training fund is financed by government and the IDA; while a payroll levy is planned, Madagascar at present provides an example of a fund that is not financed by an earmarked training levy, whether based on payrolls or otherwise.

Table 5.1
Income Sources of National Training Funds,
Selected SSA Countries

Country	Year Fund Established	Major Source of Training Funds			
		Government Budget	Training Levy		Donor Support
			Payroll Levy	Other Levy	
Zimbabwe	1984	No		--	No

			Uniform: Administered centrally		
Malawi (currently being replaced)	1972	No	--	Uniform: Administered centrally	No
Cote d'Ivoire	1977, 1992	Yes	Uniform: Administered centrally	--	Yes
Tanzania	1994	Ceased	Uniform: Administered centrally	--	Yes
Togo	1988	Yes	Uniform: Not used for training	-	Yes
South Africa	1999	Yes	Uniform: Administered sectorally	--	Planned
Kenya	1971	No	--	Sector-based levies: Administered sectorally	No?
Madagascar	1992	Yes	Not at present but planned	--	Yes

5.4 Disbursement

Chart 5.1 also shows the major destination categories for fund disbursement – sometimes referred to as 'funding windows'. Each of these four categories is aimed at distinct client groups (though there is some degree of classificatory overlap) representing an appropriate response to very different training needs and policy objectives.

The first category shown is provision of core funding to training institutions for pre–employment skills development, aimed largely at formal sector employment. We noted that government support of such training at public training institutions is a central element in conventional training markets; similarly, revenue–raising payroll levy schemes are highly supportive of this training. Training incentives may be offered to enterprises in the formal sector if initial training (including apprenticeship training) or continuing training is deemed insufficient (as discussed in Chapter 3). These may take the form of direct training subsidies to companies or, where levy–grant schemes are in place, of one of the levy reimbursement variants (discussed more fully in the following chapter).

The fund may also open a disbursement window to provide training courses for the unemployed and for special, disadvantaged groups. Traditionally, providing for the training needs of these groups has been seen as a responsibility of government, through the financing of special courses at public training institutions. Contracting for the provision of such training, following public tender that is open to both public and private training providers, is now seen as the preferred method of finance intervention (see Chapter 8). Finally, meeting the training needs of micro–enterprises and the informal sector has, in the past, been largely relegated to the workings of private markets. But as discussed in Chapter 2, these conventional private markets are not proving adequate to meet the changing needs of this growing, more technological–based sector. It is now becoming more common for training funds to offer financial incentives and subsidies for such training; for this, new financing mechanisms are being fashioned via the services of intermediary institutions (such as in Kenya). These themes are developed further in Chapter 10.

We have noted that a given fund may not cover all of the purposes indicated in the chart. The range of institutions and training forms eligible for support will usually be designated in the legislation (or other legal instrument) setting up the fund; this may be tightly defined or presented in general terms only. Which funding windows are in place and the relative size of disbursements made will depend on the particular parameters that characterize each country setting. These are related particularly to availability of income to the fund and

to the country's training needs.

The situation in many SSA countries may differ from those in other regions, in turn requiring rather different disbursement policies. In many SSA countries, the precarious state of public budgets, combined with limited income generating capacity of payroll levies, will require the government (or the governing body of the fund) to decide on strict disbursement priorities. Indeed, the introduction of payroll levies may be premature because of administrative difficulties and the relatively small size of the formal employment sector; so the fund will be more heavily reliant on government allocations and perhaps donor support. Thus, for example, levy-grant schemes (with incentives for enterprise training) have been popular – and successful – in a number of Asian countries. In contrast, the relatively small size of the formal employment sector and its lack of growth, combined with considerable growth potential for informal sector employment, may indicate the need for a different pattern of disbursement priorities in many SSA countries. Indeed, developmental needs in many SSA countries are likely to indicate that core finance for pre-employment courses at training institutions, together with innovatory methods of financing training for micro-enterprises and the informal sector, should make first call in terms of disbursement priorities. Support for enterprise training may be given less weight than it is accorded in middle-level developing countries in other continents. Whatever the merits of such expenditures, pressures on public budgets may well result in the neglect of treatment for disadvantaged groups, unless designated funding is forthcoming from donor sources.

5.4.1 Training Provision and Disbursement in Tanzania – Uneasy Bedfellows

The Vocational Education and Training Authority (VETA) in Tanzania, in its triple role as national training provider, financier and regulator, provides an instructive case where the current pattern of disbursements is not conducive to achieving the wider goals (as set out in the 1994 Act establishing VETA) of moving towards a demand-driven, cost-effective national training system.

VETA grew out of the former National Vocational Training Division (NVTD) of the Ministry of Labor; under the Act, the NVTD was ennobled with national responsibilities for all aspects of training. It is financed mainly by a two percent payroll levy, which has displaced government funding of public training provision, and also by donor support. While VETA inherited the vocational training centers of the NVTD, continuing its role as public sector provider, it was also to preside over a new decentralized, regional structure (including regional boards) aimed at meeting, more effectively, the needs of local labor markets. This would include offering support to non-government training institutions on a competitive basis.

In practice, VETA's triple role as provider, financier and overseer of the national training system has led to an internal conflict of interests in its activities. The VETA-owned, largely supply-driven, training centers, providing mainly pre-employment courses for the formal sector, dominate the activities of the regional structures; they are the recipients of the bulk of disbursements, which are not made on the basis of objective allocation criteria (see Chapter 8). In the budget for 2000, only about 5 percent of the recurrent budget (to be increased to 8.8 percent in 2001) is assigned to other, non VETA-owned, training providers (under the category 'VET provision support' which also covers informal sector training, disadvantaged groups and, in principle, enterprise training). Thus the same nominal budgetary allocation for VET support is made to each regional board, regardless of differing regional needs and the transfer by regional boards of expenditures from other budget categories is disallowed.

Clearly, the protected status given by VETA to its own training centers is grossly distorting the training market by offering training at its centers at highly subsidized rates, making it difficult for private providers to compete. This prevents moves to open the field competitively to private providers; it militates strongly against the development of open, demand-driven and low-cost regional training markets, which was a major objective of the 1996 reforms.

It will be apparent that the levy system, as now operated in Tanzania, is akin to the Latin American (revenue raising) model that is concerned primarily with the funding of public training institutions. In the VETA system, the bulk of levy proceeds are assigned to the funding of VETA-owned institutions; there are no elements present of a levy-grant system for enterprises, though formally this is not ruled out by the Act. Yet the Latin American model has been evolving over time; the model, in its pure form, has given way increasingly to a broader range of objectives, in which new activities of the fund compete for funding allocations with the traditional task of financing fund-owned training centers. We note that in the case of VETA these multiple objectives have been thrust brusquely upon a young institution, within which vested interests may have stunted the growth of these new, highly desirable developments.

The question arises whether, in the SSA context of 'instant institutional development', the financing role of national training funds can be reconciled with responsibilities for training provision. While in the traditional Latin American model the training fund (or authority) was able to accommodate these evolving roles, the VETA experience may suggest that a separation of funding allocation from provision may be more appropriate in many SSA country situations. But we must be careful to avoid a rush to judgement on this issue. In an insightful contribution (discussed in Athumani and Ngowi, 1999), Ssebuyoya (1998) comments on the difficulties that VETA is experiencing in its transition from a centralized government training department to an autonomous and decentralized authority with far broader responsibilities. Organizational change on this scale requires a new mind set from staff. Yet encouragingly, Ssebuyoya observes that while staff inherited from the former NVTD tended to be resistant to change, new staff recruited from outside were more ready to "push new and fresh ideas into the VETA system". So it is possible that this dichotomy may be transitional and resolved in the course of time.

Mauritius: Experience with the Industrial Vocational Training Board (IVTB) in Mauritius provides another case in point. It too performs a triple role – in allocating training funds (financed by government and a payroll levy), in training provision at its own centers and in regulating the training system. Bredie (1997) argues that "This is not an optimal situation ...and is bound to create conflicts of interest". The IVTB is unlikely to be encouraged to provide critical evaluation of its own training programs and, in some areas, subsidized public institutional training is crowding out private training provision. He calls for a separation of the IVTB into two agencies, one responsible for training provision, the other for the wider regulatory activities, including administering the levy–grant system and disbursement of training funds. Public training providers would need to compete for public funding on broadly equal terms with private training institutions (the proverbial 'level playing field').

Zambia: In the case of Zambia, potential conflict between the three functions of training regulation and coordination, of funding and of training provision was avoided with the setting up of the Zambian training authority – the Technical Education, Vocational and Entrepreneurship Training Authority (TEVETA) in 1998. An autonomous body with a remit to regulate and coordinate technical education, vocational and entrepreneurship training provision in Zambia, it has no training provision or funding role. TEVETA is not a training fund nor does it own or operate any training centers. With the demise of the government Department of Technical Education and Vocational Training (DTEVT), out of which TEVETA was formed, the 23 DTEVT training centers ceased to be run and funded from the public purse. The training centers are now placed under independent management boards and, according to present plans, over the longer term will need to cover costs by generating revenues from training and other activities; in the interim, staff salaries will be paid by government (Haan, 2001).

5.5 Governance, Control and Stakeholder Representation

5.5.1 Central Issues in Governance and Control

Governance varies considerably across training funds; yet the efficacy of a training fund may depend in large measure on the framework of governance and control within which it functions. Some training funds are part of broader, usually autonomous national training authorities, vested with a wide range of powers and responsibilities in the training field beyond those of financing; others are more narrowly focused funds, as discussed thus far in this chapter. There is a tendency for national training authorities to be more independent and autonomous than funds, but this is not always the case, and will depend on the legal and institutional framework in each case. Most training funds are statutory, quasi–autonomous bodies; they usually operate under the general umbrella of labor ministries and, more immediately, of a board with some degree of stakeholder representation.

The issue of governance has important implications for the successful functioning of training funds. To understand why this is so, it is necessary to answer a basic question that has not been posed thus far: why is it necessary to establish separate training funds, rather than use a designated account earmarked for training within government (the Treasury or the Ministry of Labor)? Historically, separate training funds were developed as part of training levy systems to protect the levy proceeds from encroachment by government – an issue still relevant today. But the main *raison d'être* for training funds, as such, is not merely protective. Indeed, we have noted that not all training funds derive income from levies. We may highlight the more positive reasons for establishing training funds by analogy with university funding organizations that are in place in many countries.

These organizations serve as a buffer between government and the university system; composed of university experts and relevant public figures, the buffer organizations can evaluate and plan the needs of the university

system as a whole and minimize political intervention in the allocation of funding. Analogously, management bodies of training funds can evaluate the needs and priorities of the training system as a whole (or at least that part for which it has a mandate), free from political influence. Disbursement policies and decisions are likely to be more coincident with market needs since membership of fund management bodies is usually representative of the major stakeholders, including employers and unions and also trainers. Consensus building and partnership is thus facilitated, cementing ties for cooperation on wider training issues. These benefits of autonomy are unlikely to be forthcoming where ministerial control remains strong, where governing boards are advisory rather than managerial and where they are insufficiently representative.

However, Herschbach (1990) notes that the level of government control (and the extent of board autonomy) is not necessarily linked with a greater or lesser degree of training fund effectiveness; the central issue is how, and for what purposes, control is used. He quotes the well-known Singapore case where the Vocational and Industrial Training Board, while very strongly influenced by government, yet functioned effectively to further national development goals, with training becoming a tool for the achievement of the government's policies for growth and employment. At the other extreme, government control may be highly detrimental. Not infrequently, training fund boards have been ineffective because government control has been employed "to accomplish social and political, rather than economic, objectives, have diverted funds to non-training purposes, or have exploited, rather than assisted, employers (Herschbach 1990).

5.5.2 ZIMDEF

A particularly striking case of governance shortcomings is provided by ZIMDEF, the veteran training fund in Zimbabwe. Under the 1984 Act setting up ZIMDEF (amended in 1994) the relevant minister is given overriding powers as sole trustee of the Fund. The minister appoints the chief executive (and fixes the terms and conditions of appointment), directs his activities, approves the capital, revenue and recurrent expenditure budgets. He is advised by the National Manpower Advisory Council whose mandate covers all aspects of national manpower development, not just the Fund, and its role is, indeed, purely advisory.

The Fund was set up to finance apprenticeship training (apprentice wages for the first two years and direct training costs) and reimbursement to companies of approved training. Large annual surpluses have been a feature of the Fund's activities for many years, due to declining numbers of apprentices and relatively low level of total company reimbursement payments. The latter has resulted from a very narrow definition of reimbursable training – mainly restricted to professional courses at external institutions and virtually excluding continuing training on-the-job – as well as the user non-friendly nature of reimbursement procedures. ZIMDEF does not support training for the informal sector. With the transfer of ZIMDEF from the labor ministry to the new Ministry of Higher Education and Technology (MoHET) in 1988, a change in orientation became apparent. A 'tripartite culture' – with a readiness to work with industry and a concern with labor market issues – was replaced by an education orientation.

A recent report on the Fund, commissioned by the Confederation of Zimbabwe Industries concluded that the centralization of the trusteeship of the Fund in MoHET "has resulted in inadequate capacity for the proper and effective direction and management of the Fund" (Ndoro and Durango, 2001). The authors could detect "no transparent medium-term and long-term strategic plan, which is based on the effective consultation and consensus of all stakeholders". Criteria and procedures for budget allocation were not apparent and prioritization was poor, with considerable diversification into non-core activities. Funds are used increasingly for broader purposes, such as university education and controversial investments in real estate.

The financial statements of the Fund for 1999, show that as much as 20 percent of Fund income was derived from non-levy sources, mainly from interest on short term investments from accumulated surpluses. The surplus for the year constituted 28 percent of total income (35 percent of proceeds from the levy). Less than 20 percent of training levy proceeds was used to support the apprenticeship scheme while only some 12 percent was returned to companies as grants and rebates. In parallel, property assets tripled in 1999; the value of this increase exceeded the total of all disbursements for manpower development and training in that year.

Considerable disquiet about the operations of the Fund is evident, with increasing calls for the establishment of an independent tripartite management board to oversee operations of the Fund.

5.5.3 Stakeholder Representation

Most training funds are managed by a governing board, usually operating (with differing degrees of autonomy) under the umbrella of the Ministry of Labor. Board representation is usually tripartite (government, unions and

employers), frequently (as in the case of Cote d'Ivoire) divided equally between the three main stakeholders. On occasion, additional membership is drawn from public figures from the education and training sectors.

Not infrequently, the issue of board membership composition has been a bone of contention, especially where employers have argued for greater levels of representation. Indeed, in those cases where company payroll levies provide a substantial part of training fund income, it might be both appropriate and politic that employers should feel they have some control on the uses to which the levies are put. Yet employer representation varies widely from fund to fund. In Madagascar, ten of the twelve Board of Directors of the council (CNFTP) are employer representatives while in both Cote d'Ivoire (Managing Committee of the fund – the FDFP) and in Kenya (the advisory National Industrial Training Council) employer representatives constitute a third of the membership of these tripartite bodies. In Tanzania (VETA) only two out of eleven members of the management board are employer representatives.

But even where training levies are not the main or sole source of funding, a substantial employer presence on management boards may be desirable in order to forge links with employers generally and as part of the process of fostering demand-related training: employer members of training fund boards may be seen as representing the ultimate consumers of the outputs of the training system and, as such, may have highly relevant inputs to make in board decision making. Yet overall, there appears to be no strong link between the size of employer representation on training fund management boards as such and the effectiveness of training fund management. This is not surprising. The presence of a substantial representation of employers on a training fund board does not necessarily mean that its composition is *representative* of the broad constituency of employers, generally; nor may the individuals be the most suitable for the tasks at hand. For example, as Herschbach (1990) notes: "the tendency is for larger, more politically adroit employers to be represented on Boards of Directors, and the interests of smaller employers may not be adequately addressed." He concludes that to function successfully, a number of elements must be present: a national training authority (and training fund board) "must be free of self-serving domination, by either government or private groups; it must truly represent the constituents that it serves, control its budget, and possess the autonomy to make policy and carry out decisions".

5.6 Sectoral Funds

Sectoral (industry-based) training funds offer an alternative to the national (centralized) funding model discussed thus far. In some countries, sectoral training funds, based on training levies, have been introduced in one or two sectors only, particularly in the absence of a strong national training system to cater for the needs of a strong and growing economic sector (Franz, 2000). These levies are often introduced by the industry in question. Franz (2000) discusses two SSA examples: construction in Botswana and the fishing industry in Namibia. The Botswana Construction Training Trust Fund is financed through a levy based on the value of tendered contracts; levy income, which in principle is matched by government subventions, is used mainly to finance a training center providing tailor-made courses for construction companies. In Namibia, a levy based on fish catch is used, in part, to finance a training center for the maritime professions.

Although the number of examples of the genre are limited, national systems of sectoral funding are better known, notably the short-lived industrial training board system in the UK. Nation-wide sectoral funds may be financed by a common, across-sector levy (as in South Africa since 1999) or the levy may differ by sector (as in Kenya), reflecting differing situations and needs in particular sectors.

A national system of sectoral funds offers the advantages of flexibility and the ability to focus more directly on the particular, often differing, sectoral training needs. They may be more acceptable to employers because of a greater industry-specific orientation, less bureaucracy and greater sense of 'ownership'. But the model has not been widely adopted. A system of sectoral funds, precisely because of its parochial focus, is unable to offer the broad, integrating approach to funding policy that was outlined above (Section 5.1.2). It may produce a narrow approach to training, with duplication of efforts and a failure to develop a functional approach to common core skills, transferable across industries. It is poorly adapted to meeting regional needs. Moreover it is inflexible in not allowing for redistribution of funding across sector nor for the financing of non sector-related national skill priorities or other special training programs. Hegelheimer (1986), provides a scathing critique of sectoral funds (he refers to them as 'branch' funds). He argues that they tend to result in narrow, sector-specific training; while discussed in the context of European experience, the issues raised are relevant to developing countries too.

The development of training funds in particular sectors might be appropriate in those country settings where financing mechanisms are in their infancy and are being developed on a piecemeal basis. However, and

especially within developing countries, a nationwide system of sector-based training funds has not, thus far, been seen as providing a suitable model for emulation. In this context, recent funding reforms in South Africa, to which we now turn, are of particular relevance in their attempt to develop a new national, sectoral-based funding system which both preserves the benefits of sectoral funding while avoiding some of its major shortcomings. The progress of these reforms will be followed with much interest.

5.6.1 Sectoral Funding in South Africa

The ITB system: South African industrial training boards (ITBs), recently transformed and broadened under current reforms into sector education training authorities (see below), constituted a unique feature of its training system. In terms of comparative international practice, the 27 ITBs were unusual in being sector-based and in being voluntary. These two central features have constituted built-in weaknesses to the system, militating against an effective system able to meet the needs of a changing economy. A major objective of the current reforms is to correct these deficiencies.

The voluntary nature of the ITB system led to low sectoral and labor force coverage, inefficient levy collection and under funding of formal sector training. Yet the large number of sector-based training boards, combined with a lack of central steering of the national training system, resulted in considerable under-provision of skills development to meet social needs, particularly in relation to school-leavers, the unemployed and rural populations. The system did not facilitate the shifting of resources between industries to meet the needs of emerging sectors. This is of particular concern to the South African economy, which is undergoing a process of considerable structural change, with major shifts in the composition of output and employment; these changes may be expected to intensify over time.

SETAs – new sectoral intermediaries: The 1998 Act provides for the introduction of tripartite sectoral agencies, or intermediaries, to promote high quality and relevant education and training provision at the sector level. These new Sector Education and Training Authorities (SETAs) are being developed from existing ITBs, whose functions have been broadened to include the development of sector skills plans which align to the national skills strategies and targets. SETA councils are tripartite, with an equal representation of employees and employers.

SETAs will be funded from the proceeds of a compulsory national skills development levy on enterprises (replacing the voluntary ITB levies, where in place), set at one percent of taxable employee remuneration (initially at 0.5 percent). Levies will be collected by the South African Revenue Services (in specific instances, by the relevant SETA); 80 per cent of sectoral levy income will be deposited in sectoral skills development funds to be managed by SETAs. These funds will be disbursed as grants to firms that carry out accredited training meeting criteria linked to the sector skills plan. The remaining 20 per cent of revenues will be credited to the new National Skills Fund

The National Skills Fund: The establishment of a National Skills Fund represents an important step towards providing more structured and stable funding for a range of non sector-related training activities. Levy income will be supplemented by allocations from government and by donor funds. The Fund will be used to finance national skills priorities, including employee training in priority sectors and skill categories, assistance to sectors in decline by facilitating restructuring, worker Adult Basic Education programs and the new system of learnerships (apprenticeships). It will also provide assistance to special target groups (such as women, youth, the unemployed, people with disabilities and rural communities). The earmarking of a fifth of levy income to the Fund will provide it with a more stable resource base than would be forthcoming if it were forced to compete for funding in the budgetary process. But this funding will be at the expense of enterprises rather than the tax-payer – a bone of some contention between business and government.

5.7 From Training Funds to National Training Authorities

Many national training funds are centrally concerned with the financing of training provision at the fund's training centers and/or operating a levy-grant scheme. In the latter case, training funds will need to monitor the training system to some extent; they may also provide a range of services for enterprises related to the functioning of the levy-grant system, including the consulting with enterprises in helping them develop and improve training capacity. However, in many countries national training funds are 'upgraded' to perform a far wider range of activities. Designated as national training boards or authorities (NTAs) – though sometime retaining the designation 'training fund' – these bodies are often charged with the central role of assuming responsibility for national skills development.

To respond to the developing skill needs of the economy and to be in a position to be proactive, rather than just responsive, in relation to ongoing technological and industrial change, public training systems need a greater degree of independence than is forthcoming from line ministries. NTAs will often play a central coordinating role in planning the national training system, in developing training policy, supervising national skills testing and certification as well as providing necessary information services and developing appropriate labor market signals. Independence from close ministerial control and strong representation of employers on NTAs management boards can provide the conditions for forging strong industrial links, flexibility and responsiveness and for fostering private training institutional development. Atchoarena (1996) provides an insightful discussion of NTAs.

While NTAs may not necessarily be funded by training levies, the availability of stable funding may be an important ingredient for success. Equally important is the requirement that NTAs be vested with real authority; too often NTAs lack teeth and are essentially consultative to the relevant minister, rather than executive. In Ghana, attempts to set up a national overseer body for training led to establishment in 1990 of the National Coordinating Committee for Technical and Vocational Education and Training (NACVET), an largely advisory body within the Ministry of Education and without separate legal status. In Kenya, the National Industrial Training Council is purely advisory, with little real impact; it has presided over an ongoing deterioration in public training provision (King, 2001). Following some considerable controversy, the new National Skills Authority in South Africa (discussed below), too, has been allotted a purely advisory role.

5.7.1 National Skills Development Coordination in South Africa:

In the wide consultative process that lead up to reform of the national training system in South Africa, broad agreement was reached on the need to introduce a mechanism to secure national coherence and strategic direction for the training system; the advisory status of the National Training Board (NTB) has not provided scope for these activities. The drift of discussion was moving strongly towards the creation of a new tripartite central coordinating body. Given voluntaristic traditions in the South African training sector, this body would not exercise the strong degree of central control found in national training authorities in many other countries. But it would be charged with the task of assuming overall responsibility for developing national policy, national research capacity, monitoring and evaluation studies, coordinating the activities of sectoral training bodies (SETAs) and providing them with advice and support services.

However, the government's proposals for the governance of the national training system, as set out in the Green Paper, and later formalized in the new Act, are a far cry from this scenario. The NTB was restructured into a new tripartite National Skills Authority (NSA) but employers and labor are each represented by only five of the 25 voting members. While, according to the Green Paper, the NSA will be given "much stronger advisory powers than the old NTB", it will nevertheless remain purely advisory to the Minister of Labor. It appears that under the new system the Minister, and the Department of Labour, will assume a greater degree of control over the governance of the national training system as a whole. And rather than running the important new Skills Development Planning Unit, the NSA would only have "access" to it; the Unit will be based within the Department of Labour.

In sum, under these new arrangements, union and employer representatives are provided with an advisory role only, thus denying the main stakeholders a strong role in the governance of the national training system. Instead the ministerial role was strengthened. The opportunity of creating an independent, tripartite training authority to coordinate the national training system and to assume overall responsibility for control over training development and policy, was passed by.

5.8 Training Fund Sustainability

An important objective of establishing national training funds (particularly when financed by company training levies) is to provide sustained and stable funding for the training programs they support. In practice this has not always been achieved, notably when funds do not receive the resources that have been designated to finance its activities; such an outcome not only compromises the *raison d'être* of the fund but may also call into question its sustainability over the longer term. A shortfall of funding may arise for many reasons but four are of particular note.

First, training levy proceeds, designated for the training fund, may be absorbed instead into general government revenues. This has occurred in a number of cases in SSA countries, including Gambia, Togo and Cote d'Ivoire. In the latter case, after working well for some two decades, the national training fund became insolvent and was liquidated in 1992 (Atchoarena, 1996) due to the failure (occasioned by financial difficulties)

of the Ministry of Finance to transfer training levy proceeds to the fund. The new institutional framework introduced in 1992 (including the establishment of a new training fund, the FDFP) provided for the direct transfer of levy income to a secure FDFP account.

In Gambia and Togo, the payroll levy was collected by the Ministry of Finance but rarely, if at all, transferred to the fund. In the Togo case, the levy was one of the major income sources planned for the national training fund, which was never fully operational. There appears to be a number of reasons for this, including the continuing financial crisis the country faces. But in addition, it would seem that the fiscal authorities (in Togo, as in many other countries) never fully endorsed the concept of earmarking levy revenues for training. Indeed, earmarked taxes are widely regarded as constituting a departure from sound fiscal practice, it being argued that the government should reserve to itself the right to allocate its revenues on an annual basis according to current realities and new priorities, rather than being constrained by prior commitments. Counter arguments, based on benefit grounds, can be marshaled in support of earmarked training taxes, but the case needs to be argued deliberately and clearly and consensus reached prior to implementation.

A second reason for a shortfall of income to training funds is the failure of financing bodies to meet their funding obligations. This was a contributing cause to the inoperability of the Togo fund: the European Union failed to mobilize its expected initial, and substantial, contribution to the fund. Governments too may not make the required contributions to a training fund. While the introduction of payroll levies aimed at revenue generation may be seen as a legitimate method of lowering government expenditures, the government may over-respond. Thus in Tanzania, government funding for the new training authority, VETA, which was planned to cover capital expenditures (while recurrent expenditures were to be met from the payroll levy) virtually ceased after the first year of activity of VETA.

Thirdly, where fund income is based on training levies, funding may fall short of planned levels due to technical difficulties of levy collection; this constitutes a potentially serious problem in many SSA countries and we deal with this in detail in the next chapter.

Finally, there is the problem of training fund sustainability over the longer term, in particular where training funds have been launched by donors and are funded, in the main, externally. What happens when donor finance comes to an end? The final demise of the Togo training fund was knelled with the closing of donor credit, which had been the fund's mainstay since its inception. We have noted that levy proceeds were not transferred to the national training fund; faced with severe budgetary constraints, payment of civil service salaries and debt service were seen as having prior calls on public resources. This problem of fund sustainability will be endemic in those many SSA country situations where public budgets are likely to be severely constrained over the medium term and where the time is not ripe for the introduction of training levies. In this situation, over-generous external support for national training funds, without the planned, complementary development of domestic funding, will result ultimately in moribund training authorities and empty coffers.

5.9 Lessons for Policy: Identifying Good Practice

5.9.1 Desired Objectives for Training Funds

We have noted the considerable heterogeneity in objectives and practice amongst national training funds. Yet from our wide-ranging discussion in this chapter, particularly relating to more recently established funds or those under a process of reform or redesign, we attempt to bring together various central elements of what might be regarded as desired objectives of training funds; these, in turn, facilitate identification of the common threads in training fund 'good practice'.

Ten major objectives are identified, largely reflecting the emerging consensus discussed above (Section 1.2.1); these are summarized in Table 5.2. Objectives 7–9 are discussed more fully in Chapter 8; the tenth Objective is treated more comprehensively in Chapter 9.

Limitations: In practice most SSA training funds fall short of the standards listed in Table 5.2; this is so for a number of reasons. Funds may suffer from deficient design, poor implementation or malfunction; we discuss some SSA cases more fully below. But in other cases, the scope of the Fund's responsibilities has been circumscribed purposefully; for example, the training fund in Tanzania is not concerned with enterprise training, while the Industrial Training Fund in Malawi (now replaced) was restricted to support of the national apprenticeship scheme. Factors such as limitations in institutional development, implementation capacity or funding sources may require the prioritization of efforts at the outset, moving into a broader range of

operations subsequently. As noted above, current discussions for the establishment of a pilot national training fund in Zambia indicate the desirability of funding from government and donor sources initially, only moving slowly towards the introduction of a payroll levy and levy–grant system (in line with declared government policy) at a later stage. A similar thrust is found in rather more preliminary discussions in Ethiopia.

5.9.2 Policy Implementation:

We have noted the diversity in practice amongst national training funds in SSA countries, especially in terms of the emerging consensus as outlined in Table 5.2. This is legitimate as training fund activity will need to reflect the range of objectives chosen, in turn influenced by the stage of institutional development, particular skill and human resource needs and available funding sources (including the feasibility of imposing training levies). In rare cases, a country, with more advanced training practice and an appropriate maturity in administrative and institutional development, may have moved on to set up more a fully fledged national training authority but normally this would not be apposite for SSA countries. However, whatever the given objectives and coverage of the national training fund, successful outcomes are unlikely to be forthcoming unless six key conditions are satisfied. These conditions are: security of income to the fund; fund management autonomy; stakeholder representation; a restriction of fund activities to national training needs; avoidance of the role of training provider and transparency of fund management decision making. These conditions are outlined in Table 5.3.

**Table 5.2
Ten Desired Objectives for National Training Funds**

1. National Training Funds should constitute a mechanism for augmenting and pooling resources available for the financing of training provision and for disbursing these funds to training providers.
2. Fund income may be derived from various sources, alone or in combination, including earmarked training levies (usually imposed on enterprises), government budgets, donor allocations and Fund-generated income
3. The Fund should constitute a protected source of funding for training, ideally isolated from public sector budgetary vicissitudes and thus providing greater stability in training finance over the longer term.
4. Participation of the main stakeholders (especially employers) in Fund policy formation and management, through active membership of the Fund's governance institutions, has an important role to play in building consensus on training issues; this may be particularly important where enterprise training levies are in place.
5. Depending on the defined responsibilities of the Fund, support could be available for all major forms of training – pre–employment, initial and apprenticeship training, continuing training (on– and off–the–job) and training for special groups, including minorities, the disadvantaged and the poor.
6. Funding allocation would take account of the needs of the training system as a whole and depend on agreed national priorities.
7. In principle, training finance would be allocated to all types of training providers, including public and private training institutions and enterprises providing training; ideally, attention also would be given to the special training needs of small micro enterprises and informal sector producers
8. Allocations to public and private institutional providers would be made on a competitive basis, with the aim of raising institutional efficiency, integrating training markets and moving towards demand–driven provision.
9. These objectives would be furthered through parallel policies for the decentralization of control over public sector providers and greater institutional autonomy.
10. The Training Fund would take measures to encourage enterprises to invest more in worker training, including the use, as appropriate, of various financing mechanisms including levy–grant schemes, direct subsidies and matching grants.

Primary emphasis must be given to ensuring the financial integrity of the fund. Almost by definition, the most essential ingredient for the successful operation of a training fund is security of income – that is, that fund income be adequate (in relation to the range of activities and operations expected of it) and also relatively stable. We have noted that only too often these conditions are not met. The problem may arise at two levels.

The first is at the level of the *source* of funding. Many funds are under-resourced because potential sources of income to the fund are too limited. While most funds rely on training levies, the income generated may be meager because the modern employment sector (on which the levy falls) is small or the collection system poor. Again, training levies may not be in place because they are at present unfeasible. In all these cases, the fund will need to be financed, entirely or in part, by government allocations or donor funding; yet, both of these are less stable or secure funding sources, especially over the longer term. And the generation of income from a newly-instituted training levy or the fresh availability of donor funding may displace existing government funding.

Table 5.3
Key Conditions for Training Fund Success

Key condition	Justification
1. Security of Income	Assure adequate levels, stability and sustainability of training fund incomes.
2. Autonomy & Control	Secure decision-making autonomy of management board and its control over budget allocations
3. Stakeholder Ownership	Substantial representation of the major stakeholders on management board, engendering a sense of ownership –particularly of employer groups, where training levies are in place
4. Activities (and Disbursements) for National Training Needs Only	Ensure that training fund policies and disbursements are targeted according to defined national training needs and that extraneous (non training) activities are avoided
5. Avoid Role of Training Provider	Training centers run (and financed) by a training fund tend to receive high subsidies and preferential treatment; this distorts training markets and militates against moves towards an open, competitive training system
6. Decision-making Transparency	Decision-making to be open and, in particular, the basis for fund allocation to be known and understood

Secondly, income may be insecure at the *point of transfer* to the fund, particularly where training levy proceeds remain with the treasury and are used for general budgetary expenditures rather than accruing to the training fund. Particular attention must be paid, in both fund institutional design and implementation, to the need to assure adequate levels, stability and sustainability of training fund income.

These key issues – not only income security but also fund autonomy and control, stakeholder ownership and the focus of activities of the fund – should be considered comprehensively and in detail in the early stages of fund design and not in an *ad hoc* manner during implementation. Finally, clear directives will need to be incorporated in the enabling legislation establishing the fund, to ensure that these conditions are secured.

5.10 Training Funds in Selected SSA Countries: Organization, Funding Source and Objectives

The chapter concludes with a summary presentation of the organizational structure, funding sources and fund objectives in some twenty national training funds in SSA countries (Table 5.4).

Table 5.4
Training Funds in Selected SSA Countries:
Organization, Funding Source and Fund Objectives

Country	Organization (year established)	Funding source	Objectives (and sectors covered)	Comments on the working of the scheme
Angola (planned)	National Vocational Training Agency (INAFOP). Planned –		Placement of unemployed Improving worker productivity through in	

	Employment and Training Fund		company training. Aimed at modern sector	
Benin	Planned project to put into action the National Vocational Training Policy adopted in 1998 Training fund to be established	2/3 IDA, 1/3 Government	To provide training for 25,000 workers. Modern, informal, agricultural and unemployed	
Cape Verde	Training support fund (TSF), overseen by Executive Committee and administered by Project Coordination Unit (PCU)	World Bank and Government	Development of market oriented training courses. Training institutions and enterprises	
Cote d'Ivoire	Fonds de Developpement de la Formation Professionnelle (1991), an amalgamation of the Apprenticeship Fund (1959) and the Continuing Vocational Training Fund (1977)	Apprenticeship tax (0.4% payroll) Continuing vocational training tax (net – 1.2 % payroll) Donor funding	Apprenticeship training and continuing in-service training. Support of training programs for the informal sector (sectoral cross-subsidization)	Problem of non-transfer of levy proceeds by the Treasury to the Fund (particularly in early 1990s) largely solved by establishment of special fund account
Djibouti	Planned –National Council for Training and Employment (CNFE) Never operational			
Gambia	National Council for Technical Education and Vocational Training			Levy assessed on firms but collected and deposited in Treasury – never used for training
Kenya	Industrial Training Levy Fund (1997)	Sectoral training levies (not payroll based)	Mainly formal sector: indentured learnerships and apprenticeships, skills upgrading and management courses	Levy collection and fund administration by the Directorate of Industrial Training Fall in numbers of apprentices overtime. Poor quality of public sector training (National Vocational Training Center at Nairobi)
Lesotho	Tripartite structure to oversee establishment of national guidelines			

	and TVET reform			
Madagascar	National Council of Technical and Vocational Education and Training, CNFTP. Manages Fund of Intervention for Vocational Training (FIFP).	IDA and State		Payroll levy planned for future implementation Regional and sub-regional training boards
Malawi (to be replaced)	Industrial Training Fund, (1973)	Differential head tax (on skilled workers), by skill category, in Government and private sector	Finance of national apprenticeship scheme reimbursement of apprenticeship wage and grants to technical colleges providing formal courses:	If tax shifted onto skilled workers, latter finance the costs of training apprentices
Mali	Fond d'Appui a la Formation Professionnelle et de l'Apprentissage (FAFPA)	0.5% 1 payroll levy	Fund to develop demand-driven employer-financed skills upgrading and apprenticeship training Formal (public domain); Informal (private domain)	Fund finances 75-90% of initial training costs, depending on age of trainees
Mauritania	Institutional Support Fund (ISF) Training Support Fund (TSF)	ISF financed by FAC TSF financed by IDA	ISF – to fund quality improvements developed by training institutions; TSF to finance training initiated by micro enterprises TSF – for training needs of entrepreneurs and small businesses mainly in the informal sector	
Mauritius	Industrial Vocational Training Board – IVTB (1988)	1% payroll levy. Government	IVTB training centers focus on pre-employment training. Levy-grant scheme directed to in-service training	
Nigeria	Industrial Training Fund (ITF): Governing Council fulfils role of national training authority: Industrial and Vocational Training Board	1% payroll levy plus annual budget from	Promoting employer-based training via levy reimbursement (up to about 60% of levy contribution). Some course provision at ITF training centers. Formal sector	
Senegal	National Agency for Vocational Training – ONFP (1988)	5 percent of the Fixed Contribution (employer tax of 3% of gross salaries). State grants	Formal sector training	Fully-fledged Fund is envisaged in the PDEF (Plan Decennal de l'Education et de la Formation)
South Africa	National Skills Fund (1999)	A fifth of the proceeds of a 1% payroll levy. Government contribution planned. 80% of	To meet national strategic objectives, especially long-term unemployed and other targeted special-needs groups and sectors	Fund largely controlled by the Treasury:

		levy proceeds finance sectoral training funds		
Tanzania	Vocational Education and Training Authority (VETA)	2% payroll levy	Finance of formal (mainly VETA-owned) training institutions	Regional training boards
Togo	National Training Fund (NTF)	Donors, government	Fund available for projects in the public, private and informal sectors	Payroll levy remains in the Treasury
Zambia	Technical Education, Vocational and Entrepreneurship Authority (TEVETA)	2% (suggested)		Payroll levy planned for future implementation
Zaire	A national training agency	Earmarked payroll tax		
Zimbabwe	Zimbabwe Manpower Development Fund (ZIMDEF) and also Vocational Training Fund (VTF)	1% payroll levy on private and parastatal companies	Finance of apprenticeship and other approved, mainly professional, formal sector training	Leakage to other uses: tertiary education, real estate etc. Payroll levy collected by ZIMDEF

Note: There are training funds also in: Cameroon, CEA, Chad, the Congo and Gabone

6 Training Levies

Earmarked levies on enterprise payrolls have emerged as the most widely adopted funding mechanism for financing training, both in public training institutions (usually under the aegis of a national training authority) and in enterprises. They are central to training–finance policies in many SSA countries; a number of others are currently examining the benefits and feasibility of introducing payroll levies to finance training. Given the centrality of payroll levies in any consideration of training finance, this chapter provides a detailed presentation of the types, purposes, pros and cons and efficacy of payroll taxes; the discussion is supplemented by further discussion in Chapters 7 and 9.

6.1 Alternative Training Levy Schemes

While payroll levies are the best known, and most widespread, form of training taxation, a number of countries (within SSA and beyond) has preferred to employ forms of training taxes other than on enterprise payrolls. These training taxes, not based on payrolls, tend either to be sector–specific or are introduced to finance a fairly narrow training outcome. The training tax in Malawi, now being replaced by a tax on payrolls, provides an example of the latter – a per capita tax levied on the employers of skilled workers in Government and the private sector, used to finance the national apprenticeship scheme. Examples of sector level training taxes in SSA are more readily found; to these we now turn.

6.1.1 SSA Sector Levies

As examples of sector–based levies, we have already referred to training taxes in Botswana (in the construction sector, based on value of contracts) and in Namibia (a levy based on fish catch, in the fishing industry).

Mauritius: Legislation in Mauritius provides for the collection of a one–off, lump–sum levy on each bedroom in newly constructed hotels. The rationale for this levy is that new hotels utilise skills acquired through on–the–job training at existing hotels; this construction levy would be effective payment for this if invested in

additional training; to date, however, this levy has not been collected.

Kenya: The best known scheme of this type is the Kenyan one – a national training tax system organized on the basis of eleven industry levy committees with differently based training taxes, none based on payrolls. Of the eleven industrial levy committees, eight tax companies on the basis of a fixed sum per worker; in both building and construction and in saw-milling the levy is set at 0.25 percent of quarterly turnover, while the plantations output levy is based on the metric ton. In addition, the hotel and catering levy (fixed at two percent of total net takings of hotels and restaurants).

South Africa: Under the system of separate industrial training levies in South Africa (now replaced by a standard national payroll levy), industrial training boards were equally divided between those utilizing a tax system based on enterprise payrolls and on the number of workers employed. A minority of boards levied training taxes on some other basis. In sugar milling and refining, the levy was based on output ('sugar in tons'), while the Maritime Industry Training Board was about to introduce a levy linked to turnover (replacing income on a donation basis), in the form of a 'training levy stamp' for each bill of entry submitted to customs (Republic of South Africa, 1995).

SSA sector-based schemes have met with varying levels of success and, clearly, their main advantage is that they offer a means of tailoring the levy format to the specific characteristics and needs of the sector in question. Yet the disadvantages of sectoral levies (and funds – see Section 5.6 above) remain, particularly their narrow focus obviating an integrated, national approach to the finance and planning of skills development. Thus most countries have preferred to employ standard, national-level levy schemes, based on enterprise payrolls. The rest of this chapter will be concerned with national payroll levies.

6.2 Payroll Levies: Revenue Generation

We have noted the usual division of national payroll tax schemes into two distinct groups, reflecting very different underlying objectives: revenue generation schemes (where levy proceeds are used to finance training provided by public sector institutions) and levy-grant schemes (aimed at encouraging training investment by firms themselves). However, this traditional dichotomy is becoming somewhat outdated as evolving levy schemes begin to take on a broader range of tasks, particularly in the context of the development of national training funds and training authorities. While many schemes, as we shall show, both finance public sector institutions and offer incentives for enterprise training, this distinction, nevertheless, remains a useful analytical device. There are some cases of dual-objective, mixed schemes; but for most schemes, the main thrust remains in one of these two directions.

In levy schemes within this grouping, levy proceeds are used mainly to support public sector training provision, with the emphasis on initial training at formal public training institutions. The levy scheme supporting VETA in Tanzania is of this type. The bulk of funding goes towards the finance of VETA public training centers; financial support is also provided for the national trades testing system.

In the SSA context especially, payroll levy schemes of this type may be seen as a mechanism for greater funding diversification, lightening the burden of training funding falling on the state. The expectation is that levy income would constitute a complement to existing government financing, thus providing an additional source of funding; this has not always been the case in practice (see Section 7.3.1 for a discussion of the Tanzanian experience). But there are also notable cases of the opposite tendency (as in Gambia, for example), where 'earmarked' training taxes are not in fact used for the financing of public training but rather are absorbed into general government revenues; we discuss this phenomenon in more detail below. In addition to generating more funding for training, levies of this type offer a more stable form of funding than is forthcoming from government allocations.

6.3 Levy-Grant Schemes

Unlike revenue generation schemes aimed at financing training institutions mainly in the public sector, levy-grant schemes focus on company in-service training. They create incentives for a firm to invest more in the skills development of its work force, be it in the sphere of training on-the-job (setting up or extending and improving existing company training) or by sending workers to train externally. As we noted in Chapter 3, the need for government intervention, via the introduction of levy-grant arrangements, arises because of shortcomings in the amount and/or quality of enterprise training. While there are numerous variants, Gasskov's three-fold classification of various types of levy-grant schemes has been widely adopted and is

presented here. Gasskov (1994) distinguishes between schemes concerned with cost reimbursement, cost redistribution (for which he employs the more general term 'levy-grant') and levy-exemption.

6.3.1 Cost Reimbursement

Under this category of scheme, the training fund pays grants to firms on a cost-incurred basis, for certain designated forms of training (both on and off-the-job). The purpose of these schemes is often misunderstood, particularly among employers. The scheme aims not at reimbursement of the levy as such but rather reimbursement of training expenditures incurred (to encourage firms to train more or better). Thus a training expenditure reimbursement ceiling is usually set, up to a given percentage of the levy paid. Firms that train to acceptable standards will receive back part of the levy paid, as grants; non-training firms are penalized by loss of the levy. The scheme usually could, in theory, provide for full reimbursement of the levy contribution (particularly where a large number of firms do not train and claim). In practice, reimbursement is set below the value of the levy paid, because of central administration costs and, particularly when run by a national training authority, where there are central expenditures, financed by the levy, on other training services.

Nigeria: The payroll levy serving the Nigerian Industrial Training Fund provides a veteran example of a cost reimbursement scheme. In addition to running the reimbursement scheme, the Fund finances and operates a number of its own training centers and its staff provides regular assistance to firms in identifying training needs and developing training plans (Gasskov, 1994). Because of these other calls on levy income, plus the cost of supporting the Fund's large bureaucracy, firms generally can qualify for cost reimbursements of not more than 60 percent of the levy paid; in practice, less than 15 percent of firms request training cost reimbursement.

6.3.2 Cost Redistribution

This variant differs from cost reimbursement in that it aims at redistributing the burden of training expenditures amongst enterprises. Designed in particular to deal with the ill-effects on training supply of the poaching of skilled workers by non-training firms (see Chapter 3), the mechanism provides for a sharper redistribution of levy funds, away from companies who do not train, towards those who do. Since the emphasis is on the redistribution of cost burdens, training companies may receive grants far in excess of the amount of levy paid and thus providing strong incentives for firms to train. Such cost redistribution schemes act most strongly where the bulk of levy proceeds is redistributed back to firms as grants and not used for other (albeit training) purposes.

The classic example of this redistribution mechanism is the faulted system of industrial training board levies in the UK – and particularly that of the largest of the boards, in the engineering industry. In the latter case, the training levy was set at a rate (2.5 percent of payroll), sufficiently high to result in total levy proceeds approximating total annual training investments by all firms in the industry. This sum was then distributed back to training firms only, according to particular formulae designed to measure company training efforts (Ziderman 1978).

Mauritius: There seems to be no unambiguous examples of cost redistribution schemes in SSA. The case of the levy-grant system in Mauritius is instructive because it contains elements of cost redistribution, in the sense that firms may, in principle, receive back in grants up to 200 percent of levy payments. However it is not a cost redistribution scheme because about half of levy income is assigned to support institutional training in public training centers. While the incentive scheme overall (a combination of levy-grants and company tax concessions – see Chapter 9) allows reimbursement of up to 75 percent of training expenditures, uptake has not been high, though more recently it has been rising. In the early 1990s, about 20 percent of total levy proceeds were claimed and approved for refund; this rose to about a third by the end of the decade.

6.3.3 Levy-Exemption

Arrangements for levy-exemption are usually part of broader cost reimbursement schemes, whereby firms adequately meeting their training needs are allowed to withdraw from the levy-grant system or at least to benefit from reduced levy assessments in proportion to their recognized training investments. A major advantage is that firms are freed from the bureaucratic fatigues of levy payment and grant claim and potential cash flow problems are avoided. While much discussed, this mechanism is found more typically in certain industrialized economies rather than in developing countries. They seem to be lacking in SSA countries; an exception is the Cote d'Ivoire scheme.

Cote d'Ivoire: The Continuing Vocational Training (CVT) tax is the main revenue source for the national training fund (Fonds de Developpement de la Formation Professionnelle – the Fund) in Cote d'Ivoire. Under the CVT tax, firms are required to pay 1.2 percent of payroll (in addition, there is an apprenticeship tax of 0.4 percent of payroll). Firms may receive tax exemption of half their CVT tax obligations (0.6 percent) on submission, and Fund pre-approval, of a company training plan (including training within and outside the firm), utilizing retained payroll tax obligations. Subsequently, the Fund monitors company training activity in accordance with the training plan; unused amounts are returned to the Fund. There is an additional incentive element built into the CVT system. Firms have the possibility of retaining up to an additional 50 percent of exempted payroll tax payments (0.9 percent of payroll instead of 0.6 percent). To do so, they must submit and implement training plans for three years and justify training expenditures beyond 1.6 percent of payroll; only a few percent of firms avail themselves of this possibility.

6.4 Payroll Levies in SSA

Table 6.1 presents information on SSA countries which operate a training tax regime of national scope. It will be seen that all current cases listed, with the exception of the Kenyan scheme, are payroll levy schemes; the favored levy rate is one percent of payroll. While the table assigns countries into one of the two major training tax scheme categories – revenue generation and levy-grant – it should be noted that many of the schemes, particularly levy-grant schemes, are in fact mixed ones.

Table 6.1
National Training Tax Schemes, Selected SSA Countries

Revenue Generation			Levy-Grant Scheme		
Country	Training tax	Used for training?	Country	Training tax	Used for training?
Gambia	?	No	Benin	2% of payroll	No
Mali	0.5% of payroll	Yes	Cote d'Ivoire	1.2% of payroll	Yes
Mauritius	1% of payroll	Yes	Kenya	Sectoral taxes (not based on payrolls)	Yes
Senegal	3% payroll	Very little	Nigeria	1.25% of payroll	Yes
Tanzania	2% of payroll	Yes	Malawi	Based on number of skilled workers – being replaced by payroll levy	Yes
Zaire	1% of payroll	Yes	South Africa	1% of payroll	Yes
Zambia (planned)	2% of payroll (suggested)		Togo	1% of payroll	No
			Zimbabwe	1% of payroll	Yes

Under schemes included in the revenue generation category, the Tanzanian scheme is, indeed, a pure revenue generation scheme with no allowances (at least at this stage) for levy-grant arrangements. The Mauritius scheme, however, is clearly mixed. While some 50 percent of levy proceeds has traditionally been assigned to support public training institutions, about a quarter has been reimbursed back to firms, a proportion that has been rising more recently to about 40 percent.

Most levy-grants schemes contain elements of revenue generation. Nigeria is the clearest case of dual objectives (as was noted above). The National Training Fund, established in 1971, is funded mainly by a one percent payroll levy, with additional financial support from federal government budgets (which was not forthcoming during the first decade, following its first year of operation). While the central activity of the Fund is the encouragement of companies to invest in the skills development of their employees through the offer of training grants, in 1979 it opened its first vocational training center. Though on a very much smaller scale than its levy-grant activities, the Fund has continued to expand its direct training activities.

The levy–grant schemes in Kenya, the Cote d'Ivoire and South Africa all display elements of revenue generation activities.

The Kenyan training levy –grant system is essentially aimed at financing the in–service training of workers in the industries covered. While no detailed information on the pattern of grant disbursements is published, a special exercise to identify disbursements by main expenditure category was carried out for the author, in the early 1990s. This showed that some 85 percent of disbursements went as direct rebates to companies for training expenses incurred (apprenticeship, management and overseas courses) or indirectly, in the form of fee payment to training institutions (industrial training centers and national polytechnics) for courses attended by company workers. Some 15 percent of expenditures were allocated for financing training–related matters more generally, departing from the concept of rebates. These items, normally paid out of public revenues, included the running of national seminars, fee payment and expenses of trades test examiners as well as remuneration of instructors at industrial training center skill upgrading courses leading to trade tests.

In both the Cote d'Ivoire and South African schemes, part of levy income is designated for the financing of national training activities that are usually regarded as the concern of government. In Cote d'Ivoire, some 30 percent of CVT tax proceeds (net of tax obligations retained by firms) has been assigned for financing training proposals submitted by NGOs, local communities and informal sector groups. Recently, levy funds allocated to training for the informal sector has risen to some 20 percent of Fund allocations for training (Johanson, 2001a). The cross–subsidization of informal sector training by levy funds raised from formal sector enterprises is unusual but is matched in provisions in the new levy–grant arrangements in South Africa.

As noted above, in South Africa 20 percent of the revenues from the new skills development levies on companies will be credited to the new National Skills Fund for across–sector strategic training initiatives and for the training of disadvantaged groups, activities which are generally funded from central government budgets.

6.5 Rationale: The 'Benefit Principle'

Neither public finance experts nor Treasury officials are enamored of earmarked taxes (for training or otherwise); they constrain the freedom of public officials to allocate public revenues on an annual, *ad hoc* basis according to current priorities. And many companies, claiming to see little benefit coming their way from a payroll levy scheme, point to the levy as constituting 'just another tax'.

There is now a sizeable literature (beyond the scope of this paper) that attempts to identify the essential nature of payroll levies and to seek a theoretical justification for their imposition. One rationale for payroll levies, which has been fairly widely quoted – though not necessarily accepted – sees payroll taxation as a form of 'reverse social security' (Whalley and Ziderman 1990). Based mainly on empirical literature from developed countries, it is argued that at least part of the incidence of a payroll levy is shifted onto workers in the form of lower wages. It is in this sense that a payroll levy scheme, earmarked for training, may be regarded as equivalent to a reverse social security scheme: the worker receives benefits in the form of training on entry into the labor market (or during the earlier years) and contributions are made subsequently over the working life. The relevance of this approach, even if broadly accepted, will depend on how far individual tax 'payments' match the training benefits received. This in turn will depend on how equitably training opportunities are spread amongst workers, which, of course, will differ from country case to case.

At a more pragmatic level, there probably would be wide agreement on the following proposition. Most payroll levy schemes, whether revenue generating or levy–grant, are largely used to finance training that is relevant (directly or indirectly) to the needs of the companies that pay the levy. In levy–grant schemes enterprises may claim back part of training costs incurred, while in countries where enterprise training is weak or undeveloped, levies are used to finance public training institutions which provide skills for the formal sector. In this sense, training levy schemes may be regarded loosely as examples of benefit taxation, where taxpaying individuals or institutions are major beneficiaries of the uses to which the taxes are put.

Perhaps the most quoted, non training–related, argument against the imposition of payroll levies is that, in raising the price of labor, they lead to a substitution towards more capital–using production methods and to lower employment. It is unlikely that this argument bears any weight in practice. Even where there is no tax shifting onto workers in terms of lower relative wages, a small addition to labor costs (usually only of one percent) is highly unlikely to affect wage employment significantly, except on the margin.

6.6 Coverage

Coverage of payroll levy schemes varies considerable from country to country, both in terms of sectoral coverage and size of firm included in the scheme. Most schemes exclude the public sector (Mauritius, Tanzania, for example), which results in a cross-subsidization of training for public sector employees by the private sector, to the extent that levies finance public training institutions. In South Africa, central and provincial government remains outside the purview of the training levy legislation, but government departments are required to budget one percent of personnel costs for skills development.

Size of company included in the scheme also varies. Most schemes define eligibility in terms of firm size. While the Nigerian scheme includes enterprises with 25 workers or more, most schemes seem to be more comprehensive in coverage. All enterprises are covered in the Mauritius and South African schemes, while those in Kenya and Tanzania include all employers with four or more workers. Unusually, inclusion in the scheme in Zimbabwe is defined in terms of the size of the firm's annual wage bill (20,000 Zimbabwe dollars, or over); given a monthly minimum wage of 5000 dollars, this implies that coverage is comprehensive here too.

The efficacy of such broad coverage in many SSA country schemes is questionable. In practice, the bulk of revenue is collected from the minority of large and medium-sized firms. The relatively large number of micro-enterprises, the blurred definition of the informal sector and the difficulties of small-firm identification, registration and levy collection, all combine to result in considerable non-compliance in many countries. Legislation provides for fines and/or imprisonment for non-payment in most countries; but these measures are either generally not employed (as was the case in Tanzania until the reversal in policy in this regard, introduced in 2001) or not applied to very small firms. The reason is clear: in very many cases it is simply not cost-effective to follow up on small firms through litigation or even through dispatching inspector/collectors. Zimbabwe provides a case in point. Levy income from the smallest firms covered by the levy – usually family businesses – is very small. Levy income lost from noncompliance of a very small firm may be only about 600 Zimbabwe dollars (about US\$ 12), a sum hardly justifying the costs of collection follow-up. But considerable non-compliance brings the law (and the levy scheme) into disrepute and beams negative signals to complying firms regarding continuing levy payment. A strong case can be made out for raising the minimum firm size for inclusion in payroll levy schemes in SSA countries.

In many other regions, small firms are granted exclusion from training levy schemes. The main reason for this is not only that inclusion may not be practical (in terms of levy collection) but rather because it may not be justified, particularly in levy-grant schemes. The administrative costs of applying for grants may be disproportionately high for small firms; Moreover, the training needs of very small firms differ from those of larger firms, in terms both of expenditures (in relation to operating costs) and type of training. Much of the training for which rebates may be obtained in current SSA schemes is not very relevant to very small firms (see Chapter 9).

Increasingly, financing schemes are being put in place in various SSA countries (Kenya, Ghana, for example) to deal with the needs of micro-enterprises and informal sector firms; but these tend to be based on subsidy (usually from government and donors) rather than on levy-grant approaches (Chapter 10). However, in Mauritius a voucher scheme aimed at small firms has been introduced as part of the levy-grant system. The training voucher for small businesses would allow such enterprises to recoup some of their levy contributions in an accessible way.

6.7 Levy Income Generation

6.7.1 Alternative Approaches to Levy Collection

The coverage of a levy scheme, in terms of sectors included and eligible firm size, will affect the amounts of levy income generated and, in turn, the amount of training activities it can finance. However, a factor of far greater importance in defining the size of levy proceeds, given the defined coverage of the scheme, is the method of levy collection employed. Ineffective and inefficient collection methods may result in considerable losses in potential levy income. While the literature gives much attention to the issue of the alternative uses of levy proceeds and distribution mechanisms, there has been relatively little focus on the issue of levy income generation. The essential policy question we probe here is: who should be charged with the task of levy collection? Should the levy scheme itself take on this role or should this task be assigned to a designated collection agency, usually a branch of government? Before proceeding to a discussion of the pros and cons of these alternative approaches, what may be learned from SSA county experience with levy collection?

6.7.2 Levy Collection in SSA Countries

The issues involved may best be viewed through an examination of current collection systems in selected SSA countries. Referring to the summary table 6.2, we note the division of the table into three blocks. The first two blocks relate to the use of a collection agency within government – general government tax generation mechanisms (Cote d'Ivoire, South Africa and Togo) or specialized agencies already involved in tax collection from companies, based on payroll (Mauritius and Tanzania). The third block contains examples of levy funds that collect their own levies; to this we now turn.

Self-collection: From the outset, many of the veteran levy–grant systems assumed responsibility for levy collection: these include Kenya, Zimbabwe and Nigeria.

In Kenya, the Directorate of Industrial Training (DIT) – part of the Ministry of Labour – is the implementing agency for the levy–grant scheme. It is responsible for levy collection for the training fund (in reality, eleven separate sectoral training funds) as well as administering the levy–grant scheme as a whole, with the tripartite National Industrial Training Council acting in an advisory capacity to the DIT. The DIT is officially the sole national agency responsible for training; it performs a wide range of national training functions – including running its own training centers and the national trades testing system – in addition to levy collection. Thus the DIT may be overextended. Moreover, these functions of the DIT are highly centralized; apart from the benefits this would offer in other areas, decentralization would be a useful mechanism for identifying potential levy contributors and for insuring that more contributions flowed into the fund (Ferej, 1997).

The limited company coverage of the Nigerian scheme (restricted to firms with 25 or more workers) should be expected to ease the levy collection process. However, it appears that in practice collection of the training levy imposes a heavy administrative burden on the Industrial Training Fund. Thus in referring to the relatively large Fund staff (1450 staff to service 3640 registered firms!), B.C. Mhono notes: "...the day-to-day struggle to raise levies from defaulting employers through such measures as reviewing firms' accounts, annual visits to firms, and consultancies" (in Gasskov 1994). The large geographical area covered does require a large area network of Fund officers (some 850 employees) to deliver training services, as well as collect the levy from defaulting firms (only about a half of registered firms are up-to-date with payments). The question remains whether levy collection, in this case and in others, would not be more effective if assigned to a collection agency.

Agency collection: We consider first schemes that have utilized the services of general tax collection agencies. The experience here has been mixed. The major problem has been to ensure that levy proceeds are transferred to the training fund, particularly in periods of economic difficulty and tight government budgets. In the case of Togo and Cote d'Ivoire (from 1989 until the reforms instituted in 1992) as well as in Benin and Gambia (see Table 6.1) levy funds were not transferred to the respective training funds but absorbed into general government revenues. With the restructuring of the training fund in the Cote d'Ivoire in 1992, levy proceeds have been secure; they are now deposited directly to the Fund rather than to a Fund account in the Treasury. Tanzania is moving towards levy collection by the Tax Revenue Authority (see below)

The new levy system now being introduced in South Africa, however, also uses the tax system (South African Revenue Service – SARS) as the collection agency, with levy proceeds being deposited initially in the Treasury (National Revenue Fund – NRF). The Minister of Labour then instructs the NRF to distribute levy proceeds to the new National Skills Fund (20 percent) and 80 percent to the Sector Education and Training Authorities – SETAs, responsible for training in each sector. Levy proceeds from companies not attached to a SETA are assigned wholly to the National Skills Fund. In theory, the use of the NRF as a depository might render levy proceeds less secure in periods of pressure on public budgets. The reform does allow for the possibility of individual SETAs collecting the levy from firms in their sector (and passing on 20 percent to the National Skills Fund); this would remove the possibility of central leakage of levy income to non-training uses. However, thus far, levy collection has not been delegated to any SETA.

In many ways, the use of a government department, already charged with the collection of a levy based on payroll, would appear to be the most effective collection method. But, again, experience is mixed. In Mauritius, the collection of the payroll levy appears to be extremely efficient. The levy is collected monthly by the National Pension Board, on behalf of the Fund, as an add-on to the larger national pension insurance contribution. The simplicity of this system, and the high incentives to report non-payment of pension contributions, ensure a very high rate of compliance (estimated at 96 percent). Experience in Tanzania is less positive, particularly in terms of levy compliance.

Table 6.2
Levy Collection Systems: Selected SSA Countries

Country	Collection Agency	Collection Fee (% of levy proceeds)	Initial Disposition of Levy Proceeds
Cote d'Ivoire	Tax Department, Finance Ministry	?	Previously deposited in a Treasury account; now levy proceeds transferred directly to outside training fund account
South Africa	South African Revenue Service – SARS	2 %	SARS pays levy proceeds into National Revenue Fund. Minister of Labor allocates proceeds between the National Skills Fund (20%) and sectoral training bodies (SETAs –80%)
Togo	Ministry of Finance	–	Absorbed into government revenues; not transferred to training fund
Mauritius	National Pension Board	4 %	Transferred to training fund
Tanzania	National Social Security Fund (soon to be replaced by the Tax Revenue Authority)	7.5 % (previously 5 %)	Transferred to training fund
Kenya	Self collection (Department of Industrial Training)	–	Direct to training fund administered by the Department of Industrial Training, Ministry of Labour
Nigeria	Self collection	–	Direct to training fund
Zimbabwe	Self collection	–	Direct to training fund

The debate in Tanzania – agency vs. self-collection: The National Social Security Fund (NSSF) has acted as the levy collection agency for VETA, the Tanzanian training authority since the establishment of the levy scheme in 1995 (falling on all companies of four or more workers). It is widely felt that the NSSF performance has been sub-standard; this view has acted as a catalyst for calls within VETA to rescind the agency arrangement and to establish its own levy collection unit. A brief review of this local debate may prove useful in highlighting some of the wider, general issues surrounding the relative advantages of self-collection and the use of a collection agent.

In recent VETA internal report (the Report) arguing for the establishment of a levy collection mechanism within VETA (VETA 2000), the main thrust of the argument against the NSSA is twofold: that it has not proved effective as a collection agency and that VETA could do the job cheaper. Neither argument, however, is proven.

The report claims that the NSSF gives second priority to training levy collection, which is not its central concern. In theory, this should not arise since the NSSF, in collecting the NSSF contribution, will contact automatically employers also eligible for the training tax; however, NSSF inspectors are not always knowledgeable about the workings of the levy and may not be persuasive in eliciting payment from recalcitrant firms. The NSSF now receives a commission of 7.5 percent on all collections, representing a Ministerial-imposed compromise between the 15 percent claim advanced by the NSSF (later reduced to ten percent) and the former rate of five percent. So the NSSF may be a less than willing partner, here. NSSF proceeds from its 20 percent levy on wages (comprising employer and worker contributions) are in the order of 70 billion shillings. Pro rata, the two percent training levy would result in 7 billion shillings (or somewhat less, because payment to the NSSF falls on all employers) and not the 5.2 billion shillings actually collected.

The report refers to an employer compliance rate of 20 percent and to collection of only 22 percent of potential levy proceeds, estimates far short of NSSF claims. However, while the report's estimates may be formally correct, they do not provide a full picture of the situation, since only about 28 percent of employers have registered for levy payment. In terms of registered employers, almost 70 percent of employers comply with

levy payment, producing some 88 percent of potential proceeds. On the face of it, this seems to produce a better outcome than levy self collection in Zimbabwe where, we have noted, only 60 percent of registered companies pay the levy (of which 10 percent are in arrears).

The problem in Tanzania, then, is essentially one of low registration; this may reflect inefficiencies of the NSSF collection mechanism or may be the consequence of insufficient incentives in the form of a commission rate that is far below that which the NSSF claims is reasonable. Yet, lower agency fees are charged in Mauritius and South Africa (Table 6.2). The question arises: could VETA do the job cheaper – and better – than the NSSF? The report presents an internal (and therefore perhaps optimistic) exercise that estimates a self-collection cost of only about 27 percent of the projected agency fee (about two percent of proceeds). The proposal for self collection, however, was rejected by VETA's national board, reversing initial approval. Arguments against the proposal include the risk that the core activity of VETA may be neglected as the administrative weight of levy collection diffuses attention away from training and also the lack of administrative capacity of VETA regional offices to undertake collection.

Finally, one advantage of self collection in levy-grant schemes (as in Zimbabwe) is that collection inspectors also double up as 'PR officers', and can play a potentially important role in explaining the rebate system and encouraging firm to apply. This issue is not applicable for the Tanzanian revenue generation scheme.

The debate has now been over-ridden by a unilateral decision of the Ministry of Finance, to charge the Tax Revenue Authority (TRA) with the responsibility of levy collection. Under new legislation, the TRA will now collect a new combined "skills and development" levy, based on six percent of payroll; two thirds will accrue to the Treasury and one third will pass directly to the training fund. Given pressures from the Treasury to secure maximum public general revenues from this source, it is expected that the TRA will collect the levy more vigorously, particularly in terms of employer registration and follow up on payment default.

Clause 19.2 in the new legislation seems to tilt the source of power and control over the levy strongly towards the Ministry of Finance. Under this clause, it is the Minister of Finance (rather than the Minister of Labour) who will now "make regulations relating to the collection of the levy". More important, under that clause, are the new powers given to the Minister of Finance to make regulations concerning the *distribution of the levy*. This could carry dangers for the security of the use of the levy for training purposes; until now, decisions on the use of levy funds were made by VETA and not the government. And an open question remains whether the joint collection of the two levies under a common framework will not endanger the security of VETA income over the longer term.

6.8 Payroll Levies: An Over-Sheltered Source of Funding?

We have noted a number of cases in SSA where the payroll levy system has not resulted in more training, as levy proceeds have been dissipated into general government revenues. This is the case in Gabon, Togo and, for a period, in Cote d'Ivoire, leading to a collapse of the respective training funds that they financed. But more usually, payroll taxes have been a stable form of funding for training in SSA countries. But usually these taxes have brought additional funding to the public sector and, in many cases, they have been a useful device in offering incentives for the development and strengthening of enterprise training.

However, training taxes may constitute an *over-sheltered* source of funding leading to unspent surpluses (Dougherty and Tan 1991). The Zimbabwe scheme has resulted in income generation far in excess of cost reimbursement demands, leading to questionable forays into fields very loosely related to the objectives of the scheme. Surpluses generated by the scheme in Mauritius have led to a drastic cutting of complementary government funding for the training fund. The initial levy rate may be set too high, especially in the case of cost reimbursement schemes or a rate that may have been appropriate at one time is not revised downwards as financing needs change. In Nigeria the levy rate, initially set at three percent in 1971, was reduced subsequently to the current rate of one percent four years later. Surpluses may lead to inefficiencies and top-heavy bureaucracies; alternatively they may lead to the use of payroll tax revenues for purposes other than training. Herein lies the role of strong controlling boards, representing the major stakeholder interests, to monitor the system and to ensure that abuse does not ensue.

The root of the problem, however, arises from the arbitrary way in which levy rates are fixed and in the inflexibilities of the system (with the tax rate often enshrined in the legislation setting up the scheme). In the initial stages of setting up a scheme, only too frequently the levy rate is fixed arbitrarily. Often, the pragmatic approach adopted is to ask how much the system (i.e. employers) will bear and to emulate current rates in other countries, rather than to estimate revenue needs (which may change in the future), from which an initial

tax rate is derived. This highlights the basic dilemma: how may a payroll tax system be fashioned to be flexible enough to respond to changing expenditure needs (and avoid surpluses), without forgoing the benefit of stable funding? It would be advisable to include within the enabling legislation a requirement to review the levy rate periodically (say every four to five years) but to guarantee a stable levy rate between revision dates.

6.9 Lessons for Policy

6.9.1 Training Levies: Strengths and Limitations

Training taxes, usually levied as a percentage of company payrolls, are now established throughout the world as the most pervasive mechanism employed for funding training systems (Whalley and Ziderman 1990). Training levies have been introduced in many SSA countries and are on the policy agenda in a number of others. But the success record of training levies in SSA countries appears to be less than in other regions; while working well in some SSA countries, training levies they have been found to be wanting in others. In this policy-oriented chapter, we draw up a balance sheet, setting out the strengths and advantages of training levies against their possible dangers and limitations (Table 6.3). This listing (based on National Business Initiative 1995) is then followed by a discussion of key issues in training levy design and implementation that may be crucial factors in augmenting the benefits to be secured from training levies, while limiting – if not some eliminating – some of their weaknesses.

Table 6.3
Payroll Levies: Advantages and Limitations

Advantages	Limitations
Diversifies the revenue base for financing training, by mobilizing additional revenues	Given their particular training needs, many firms, particularly small ones, do not benefit from the scheme; this breeds resentment, opposition and compromises the status of training levies as "benefit taxation"
Can provide a stable and protected source of funding for national training provision; this is particularly important in the context of national budgetary instability	Earmarked taxation do not conform well with the principles of sound public finance and weaken attempts to unify the national tax system
Where forming part of a levy-grant system, can encourage firms to intensify their training efforts, increase training capacity and raise training quality	Under fiscal pressure, government may incorporate training levy proceeds into general public tax revenues
A strong case can be made for viewing earmarked payroll levies as "benefit taxation"	Levy proceeds may be diverted to non-training uses
Training levies collected from formal sector employers can serve as a vehicle for cross subsidization of training, especially from the formal to the informal sector	Payroll levies may constitute an over-sheltered source of funding, leading to unspent surpluses, inefficiencies and top-heavy bureaucracies
	Payroll levies raise the cost of labor to the employer, possibly discouraging employment
	Employers may shift the incidence of the levy on to workers in the form of lowered wages; in this case, workers and not the employers bear the burden of the tax

6.9.2 Issues in Levy Scheme Design

Table 6.4 summarizes a number of crucial issues in payroll levy scheme design and implementation; failure to pay due attention to these issues is likely to compromise the prospects for successful operation of the payroll levy scheme.

Table 6.4
Issues in Levy Scheme Design and Implementation

Issue	Commentary
Levy rate	Levy rates to be subject by law to periodic review to avoid accumulation of surpluses
National or sectoral levy rates	A standard, national payroll levy rate (rather than differing sectoral rates) will be most appropriate for most SSA country situations
Sectoral coverage	Levy coverage should be as wide as possible across economic sectors and to include public enterprises, NGOs etc.
Company size	Very small firms should be exempt from levy payment, on both efficiency and equity grounds
Levy collection	Levy collection should be placed in the hands of effective agents; self-collection by funding organization to be avoided
Security of levy proceeds	Special attention should be given to guarding levy revenues from raiding by the government (especially where tax authorities act as the collection agent), by placing in special, closed accounts
Employers buy-in	Employers should be involved in payroll levy policy formation and execution
Avoidance of premature introduction of payroll levies	Payroll levies may be inappropriate where levy-income generating capacity is weak – either because of the limited size of the formal sector or administrative/organizational difficulties of levy collection

7 Finance Mechanisms: Augmenting Funding for Training

7.1 Funding Augmentation v. Funding Distribution

Two central financing issues are common to all training systems. The first concerns the pressing need to augment the total amount of funding for public sector training, in the light of a paucity of government funding, in part the result of the adoption of structural adjustment policies and increasing calls on government funding from competing sectors. The second relates to improving the efficiency and effectiveness of national training systems, to enable them better to meet the needs of society and the economy. Governments have increasingly turned to the use of various financing mechanisms – some well established, others largely experimental – to move towards these objectives.

Policies for augmenting the amount of resources available for training programs may entail a combination of such measures as greater funding diversification, reduced government training subsidization and the increased sharing of the training finance burden by other beneficiaries of the training process, particularly trainees and enterprises. Funding mechanisms that lead to better training outcomes and other national policy objectives usually, but not only, relate to the allocation of training resources and transfers within the system. This distinction between financing mechanisms that increase the total amount of funding resources available to the training system as a whole and those mechanisms that allocate given funding resources (Johanson 1995) is useful for gaining a better understanding of the objectives and functioning of various training finance mechanisms. However, the distinction should not be pressed too far and is best seen as a useful, but not perfect, pedagogic device. Some financing mechanisms relate both to augmenting finance resources and to their transfer within the training system (for example, training levies), while others do not fit tidily into either category.

With this caveat in mind, in this chapter we discuss mechanisms aimed at funding augmentation; the focus is on augmenting funding for institutional training. Following chapter deal with funding distribution.

7.2 Funding Diversification: Alternative Approaches

In national training systems where public training budgets are constrained, it is usual practice to seek alternative or additional funding for public training from other sources: a process that is referred to in the literature as funding diversification. The process is outlined in Chart 7.1.

The left-hand-side of the chart illustrates the situation where public sector training providers, the dominant suppliers of institutional training, are funded by public budgetary allocations. The introduction of funding diversification may take different forms. The chart identifies four main avenues that may be pursued, separately or in parallel; three are direct and one is indirect.

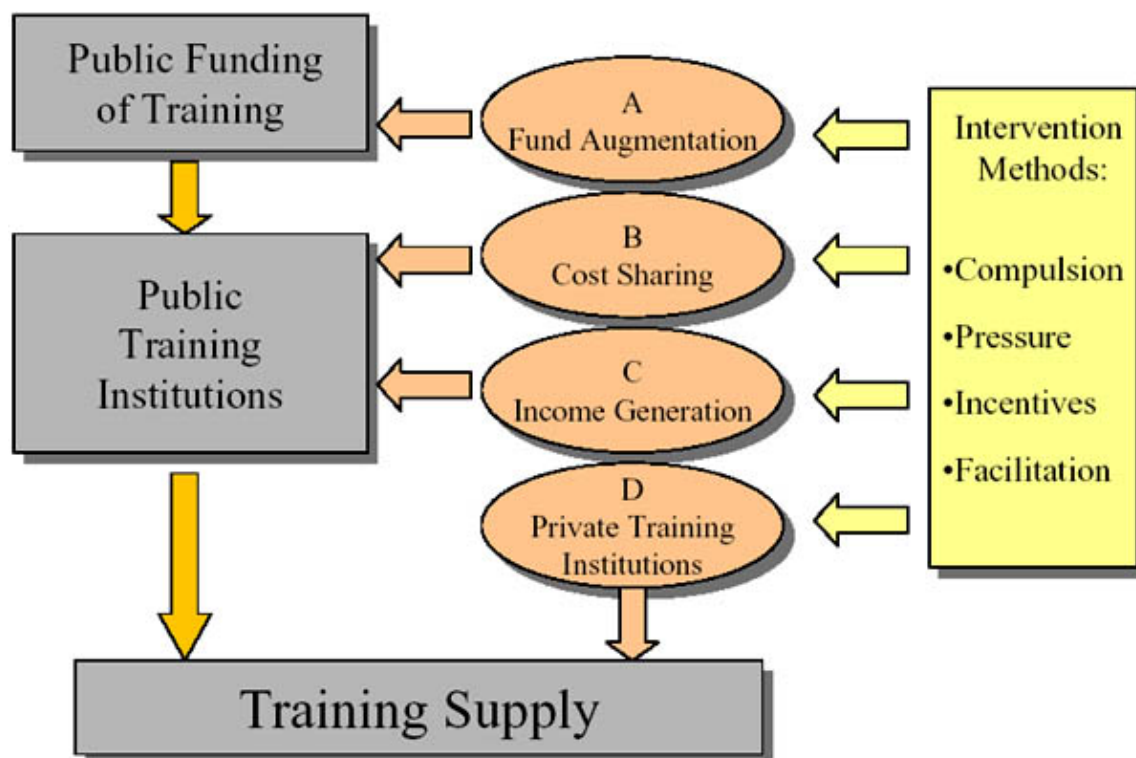


Chart 7.1 Financing Training Institutions Funding Diversification

First, as shown by ellipse A, public sector training funds available for the support of training institutions via subventions, may be augmented from other sources; the classic method is to impose special taxes, earmarked for training. Here the size of the pool of funds available for distribution to training institutions is augmented but there is no immediate effect on the income of individual training institutions. The second approach (ellipse B) is to lighten the weight of training finance falling on public funds, through the introduction of cost sharing with the beneficiaries of training. This is achieved mainly by introducing training course fees or by raising them to more realistic levels. These measures will allow a reduction in public subsidies for training or the provision of more or better training services with given levels of public support. User fees could be used also to augment public financing, such as through payment for needed quality improvements or even basic supplies, without reducing public financing. In these cases, there is a direct change in the sources of funding for the core training activities of the institution, with trainee fees partially replacing public funding (but not always, as we shall argue below). Third, (ellipse C), training institutions may seek additional income from other sources, such as selling of products or renting out of facilities. In this case, income generation, if sizeable, is not related directly to the institution's central core training activities (see below).

A fourth, indirect, method of generating funding for training (and, in parallel, reducing the call on public funds) is through the development of private training institutions – ellipse D. This approach may be particularly relevant for country cases where expansion of the training system is desirable. Expansion can be achieved through the growth of private, rather than public, training provision, without large commitments of public funds. We discuss each of these four methods in turn.

7.3 Fund Augmentation

7.3.1 Training Levies

We have noted in Chapter 6 that many countries now use special training taxes to generate funding for the public financing of training. Earmarked training taxes, levied on the payrolls of enterprises, have emerged as the most widely adopted alternative to government budgetary allocations. In many cases, the declared intention underlying the introduction of a payroll levy is to lighten public sector financing burdens. However, there remains the danger that, due to funding pressures from other areas of government activity, this process may be taken further than intended.

Levy income drives out government funding – Tanzania: The Tanzanian levy provides a case in point: levy income has displaced government funding of capital and development expenditure. Under the Strategic Action Plan accompanying the establishment of VETA and the Tanzanian training levy, it was envisaged that government would no longer fund recurrent public training expenditures. Operational expenses to run the new system would be borne by revenue generated through the system's own resources – levy income, fees and other generated income. However, capital and development expenditure would continue (for the foreseeable future) to be funded by government and donors; indeed, continuing government funding support is envisaged in the Vocational Education and Training Act (1964). Government found it expedient to opt out of public financing of training altogether, passing the onus of capital development funding onto VETA. Moderate government contributions to capital development were forthcoming for the first two years of operation; in 1997, government allocations to VETA were phased out completely. Concurrently, donor contributions are being scaled down and constitute only about 55 percent of budgeted capital and development expenditure for the year 2000; the shortfall is provided from VETA internally-generated revenues, rather than from government allocations.

Levy income complements government funding – Mauritius: The Tanzanian case may be contrasted with more positive experience in Mauritius. Here also, the major part of the levy raised is used directly by the Industrial and Vocational Training Board (IVTB) for its own training programs. But the government matches, from general revenues, employer levy contributions to the IVTB for recurrent expenditure, and pays 85 percent of capital expenditure by the IVTB (Dar, Gill and Bredie, 1997); donor funding is minor. Thus, during a period of major IVTB expansion, it was the government that provided the bulk of IVTB overall funding directly, through general government revenues. This situation may now be in a process of change, because of the accumulation of non-refunded levies (traditionally only about a quarter of levy income was redistributed back to companies, though this has risen dramatically more recently). Beginning in the financial year 1997/8, the IVTB was called upon to use part of its considerable reserves; as a result the government contribution has fallen substantially. In 1998, the government contribution was set at a token level only, as a signal to the IVTB that it should reduce substantially its accumulated reserves. With the rundown of accumulated fund surpluses, the way is open for renewed government financing.

Levy income replaces government subsidy of enterprise training: Although this chapter is focussed on augmenting funding for training institutions, training levies may lighten the burden of training finance falling on public budgets in a rather different way. We have noted in Chapter 3 the tendency for enterprises, particularly in the formal sector, to under-train. In response, the state may provide a framework of training subsidies (for initial training, including apprenticeships, management courses and continuing training more generally), thereby offering incentives to enterprises to train more and better. Levy-grant mechanisms offer an alternative funding source for these training incentives, with the government-financed training subsidy being replaced by (compulsory) enterprise-funded training grants/cost-reimbursement (see Chapter 9 for a further discussion).

7.3.2 Provision of Training Services

A training fund may generate limited additional incomes through the provision of services, for payment, to enterprises; these include consultancy, the development of training manuals, training promotion, advisory and other services.

7.4 Cost Sharing

Unlike fund augmentation, which results in a larger funding pool, cost sharing aims at reducing the size of allocations to individual training institutions. A general approach, which seems to be more prevalent in advanced rather than developing economies, is that of matching funds. However, the best known and most widely used method by far, is the imposition, or raising the level, of user fees to trainees or students enrolled

in training courses.

7.4.1 Matching Funds

The use of matching funds (often referred to as co-financing) requires that the institution in receipt of public funds assumes responsibility for raising part of training costs, particularly for capital investments. Thus not only do institutions receive less than full funding from budgetary sources, but they are also obliged (as a condition for the receipt of public allocations) to finance some proportion of training from their own sources. This approach does not specify how this funding should be raised and the most straightforward approach is for training institutions to pass on the non-subsidized portion of training costs to the beneficiaries in terms of fees. But institutions may also respond to co-financing arrangements by generating income from other sources (see below), though this is not strictly cost-sharing.

Matching funds not only supplement public funding; they may also encourage local initiative in funding generation, with local institutions that wish to receive government funding embarking on revenue generation activities (Bolina, 1996). The approach offers flexibility, with the option of varying the proportion of required institutional matching by region, institution or course offering in line with defined policy (Jager and Buhner, 2000); also the matching proportion may be raised over time, as institutions gain strength in revenue generation.

An indirect, and non-obligatory, variant to co-financing is available; while it is rather different in conception, similar end results may be achieved. Institutions are provided with less than full budget allocations (based on standard costs elements) and are thus under pressure, though not obliged, to supplement income from other sources. This approach underlies the budgeting of public training institutions in Tanzania, discussed below (Section 7.8).

7.4.1 Cost Recovery: User Fees

It is almost platitudinous to point to greater cost recovery for training courses – the use of user fees – as the most readily justified mechanism for funding diversification. The logic is clear. It is highly legitimate to require trainees to bear at least a part of the costs of training when skills acquisition is seen as an investment in human capital, with the promise of higher labor market earnings and a greater probability of sustained employment. Many SSA countries, including Malawi, Madagascar, Mauritius, Nigeria, Tanzania, Zambia and Zimbabwe, have introduced fees for training courses. Fees are usually set at symbolic levels only; fee income accruing to the Industrial Vocational Training Board in Mauritius accounts for only one–two percent of revenue. However, in some cases fees are more substantial, even though still very far from full cost-recovery. In public training centers in Tanzania, fee levels are about 15 percent of recurrent costs; in Madagascar, 27 percent.

The efficacy of cost recovery through user fees will depend to no small extent on overall training fee policy. We may discuss user fee policy within two very different contexts. A central body, whether government or training authority, may impose standard user fees, across training institutions. Alternatively, training institutions may be granted the freedom to introduce, and fix the level of, fees for training courses provided. While both produce the desired effect of greater cost recovery and of lowering pressures on public budgets, they carry very different implications for the management, and functioning, of training systems.

Standard, nationally set compulsory fees (as are in place in public training centers in Tanzania, for example) are unlikely to reflect local market realities. They obviate the use, by individual institutions, of user fee policy as a management device, especially in terms of marketing various available courses to client groups with differing needs. Centralized fixing of standard fees is also an inflexible tool; it does not allow the local institution to vary fees, to reflect changing local market conditions.

In cases where user fees are voluntary and left to local institutional initiative, they may encourage training providers to develop a more dynamic, even aggressive, approach to exploiting the potential of the local market environment. In this way institutional fee policy becomes more than a device for cost recovery and cost sharing: in providing a mechanism for varying fee levels across courses and client groups it serves as a tool for moving the training system towards an environment characterized by open, demand-oriented training. However, there is an important proviso here and this is that local training institutions should be free to retain user fee income and the sums collected should not be deducted from institutional budgetary allocations. In many cases, this condition is unmet: in Zambia, fees collected at the technical training institutes, while easing the immediate cash flow, do not add to net institutional income. More generally, it is recognized that fee policy is not set in a vacuum. Institutional-level fee fixing is usually but one element (ideally a central one) of more

general, decentralized training systems with local institutional autonomy. It is only in this more liberal context that the full potential of cost sharing is likely to be forthcoming.

Finally, the positive financial benefits from greater cost recovery need to be examined alongside the potentially adverse effects on equity. Higher, realistic fees will exclude from training those who are unable to pay; fees set at comfortably low levels will fail to make a sizeable contribution to cost recovery. In particular, negative impacts on the access to training opportunities of the poor, minorities, rural populations and other disadvantaged groups are likely to ensue. This points to the widely recognized need to introduce targeted subsidies directed to these at-risk groups, in the form of scholarships and reduced fees. However, targeting those *most* in need within these groups, particularly in the SSA context, has proved to be no easy matter. A form of creaming is likely to result, as subsidies reach more readily those who are less obviously in need, on the margin of the eligibility threshold.

7.4.2 Trainee Loans

Cost sharing schemes, through the use of user fees, are likely to be burdensome not only for the poor, thus discouraging participation in formal training programs; this is particularly so if fees are set at a sufficiently high level to achieve significant cost recovery. The classic solution to this problem, encountered most frequently in higher education, is deferred cost recovery (Albrecht and Ziderman, 1991). Loans can provide students with the means to pay tuition fees (and living expenses); thus they ease student payment burdens during study by enabling them to delay payment until they are in receipt of the higher earnings that the education course has made possible. In similar fashion, there is increasing support for the use of training loans schemes, as an adjunct to raising fees for training programs; however, more sober reflection militates against this (Herschbach 1993).

There are a number of reasons why training loans (which have been introduced in a number of Western countries, including the UK) are unlikely to be appropriate for SSA training systems. The track record for student loans schemes, particularly in SSA countries, is poor. Student loans schemes, introduced in Kenya, Tanzania and Zimbabwe for example, have all resulted in very low loans recovery, due largely to overly generous repayment conditions, including below-market rates of interest, repayment in nominal terms and long grace periods. In addition, given the presence of administrative costs and repayment default, a regime of student grants may be more cost effective than loans. The sound administration of a loans scheme requires appropriate, high level, institutional support – at a premium in many SSA countries. Given the lack of success in administering student loans scheme in SSA, it is improbable that training loans would fare better. At present, they do not appear as a realistic option over the medium term.

7.5 Income Generation by Providers

7.5.1 Income from Production

In many training programs, income is generated from the sale of production and service activities of trainees. Such income generation may take many forms. Income may be derived from the training process itself. This could be in the form of the provision of services (such as car repair or hairdressing services), which also offers trainees valuable practical experience gained from working with real clients. Or items produced as part of training may be sold. Income additions are likely to be marginal from these sources.

But it is possible, more purposefully, to utilize available skills and facilities to produce output for sale in the local market. While the concept of combining learning with practical experience is maintained, the issue becomes one of balance between these two activities (Herschbach 1993). As more weight is given to instruction, the income potential from production declines. Alternatively, quality of training might suffer as emphasis is placed on production rather than instruction. Against this, however, exposure to local markets may lead to more relevant, market oriented training.

The proportion of recurrent expenses that can be covered by production sales may vary considerably from case to case; but while there are some exceptions pointing to the contrary, the scope for cost recovery here is usually fairly limited usually accounting for only a few percent of recurrent expenditure. In some cases, however, it can contribute a considerable proportion of total costs; Herschbach (1993) suggests as much as 80 percent for Swaziland. In the case of the Botswana Brigades, training with production has been able to recover, on average, 20 percent of total training cost (Franz et al 1998). The recovery potential for the Brigades has not been fully exploited; Franz (2000) assesses this to be in the range of 25–35 percent of total costs and in exceptional cases even higher. But a major objection, often voiced in relation to the Botswana

Brigades is that training institutions may be competing unfairly with the local companies, because of their low labor–input costs (Franz 2000).

As with training fee policy, local initiative in income generation from production will be stunted if this income does not contribute to institutional budgets. In Zimbabwe, for example, income from production accrues to the training fund, not the training institution.

7.5.2 Sale of Services

Training institutions may generate income from the sale of services, including the renting out of underused facilities and providing consulting services to local enterprises.

7.6 Encouraging Private Provision

This chapter is concerned with the financing burden falling on government in supporting public training institutions; why is private training provision important in this context? Responding to pressures for the expansion of formal, institutional training provision will require sizeable increases in public expenditures. These increases, we have argued, could be contained by additional, offsetting revenues generated from increases in course fees at public training institutions.

A complementary measure is to encourage the growth of private training institutions, with trainees paying full costs. In this way, expansion of the national training system can be achieved but through the growth of private, rather than public, training provision – and without commitments of public funds. Indeed, if there are financial constraints holding back private institutions' development, it may be cost–effective for the government to provide public subsidies to these institutions, as a way of facilitating national training provision with a minimal burden on the public purse (or, at least, at lower cost than expansion of the public training system). In addition, of course, *reduced* public training provision could be possible (and concomitant budgetary reductions) with the reduction in public training supply made up by compensating expansion of private training institutions.

In many countries, the lack of private training provision results from financial, institutional and other constraints, holding back private provider development. We have noted in Chapter 3 that training provision in public training institutions may be a justifiable response to a lack of private training providers. But in some countries this lack of development in private training supply may be more a response to government training policy, than it is its cause. Thus despite the important role that private training institutions can play in meeting growing demands for skills training, governments often treat these institutions with a large degree of skepticism.

The imposition of restrictions such as legal prohibitions, tight regulatory control and tuition fee ceilings may combine to render private institutional start–up very problematic. While these restrictions are intended to protect the interests of potential trainees, they are often counterproductive in constraining private training supply. What is required is a more liberal regulation regime, particularly aimed at quality control, combined with an enabling environment encouraging the flowering of incipient private training institutions

In considering steps that governments might take to encourage private institutional training supply, it is necessary first to pose the question: why is private provision not forthcoming? What are the constraints? We discuss these issues in the paragraphs that follow.

7.6.1 Measures for Building Up Private Training Capacity

We may identify four types of constraints that may hold back the development of private training institutions: these are financial constraints, issues of fees policy, regulation and control of private training institutions, and information gaps.

Financial constraints: The large majority of private training institutions in SSA countries offer courses in commercial and business occupations, with comparatively low capital costs and a relatively abundant supply of instructors. However, costs at technical and industrial courses are higher, particularly for capital development;

Fees policies: Imposed tuition fee ceilings, while aimed at protecting trainees from exploitive activities by private training institutions, may too rigidly limit the ability of these institutions to enter new training markets,

especially those with high investment and recurrent costs. Moreover, tight (low-level) fee control may produce the undesirable effect of low cost, low quality training.

**Table 7.1
Constraints on the Development of Private Training Capacity**

Constraint	Mitigation
Financial	To offset limited capital market access, offer development loans/subsidies
	Provide subsidies for equipment and staff development
Fee policy	Avoid imposing protective training tuition fee ceilings, without good cause
Regulation	Be sparing in regulatory and enforcement policies
Consumer Information	Provide good information to potential trainees on the quality of institutions and course offerings
	Provide updated information on relevance of courses to labor market demands and opportunities

Regulatory environment: Private training institutions are unlikely to flourish in an overly strict regulatory environment. Regulation is no doubt required against the possibility of dishonest practices, excessive advertising and training of low-quality. However, regulation and enforcement should be sparing; while sufficiently robust to counter excesses, they should be designed to encourage private training institutions to operate fairly and efficiently within a facilitating, regulatory environment.

Consumer information: Without reliable information, consumers are unable to make wise and informed choices. But relevant information on private training institutions is often lacking. This lacunae may provide an opportunity for effective government intervention in providing potential trainees with information on both the quality and stability of private training institutions. Provision of updated information on the relevance of courses to labor market demands and job opportunities is also important.

7.7 Role of Government: Four Intervention Modes

From the foregoing discussion, it is noted that significant funding diversification does not take place in a vacuum. There is a role for active government policy in the development of all four methods of funding diversification. Yet government moves to increase funding diversification may take a number of forms; we find it useful to distinguish between four intervention modes, on a continuum of decreasing government intervention – compulsion, pressure, incentives and facilitation. The relationship between intervention mode and method of funding diversification is mapped in Table 7.2 (see also the right-hand side of Chart 7.1). It is noted that there is a clear relationship between government intervention mode and the method of funding diversion that is employed. Those cases, where there is a strong effect of a given intervention mode on funding diversification method, lie on or near the diagonal in the table.

Training taxes, whether levied on company payrolls, output or other measure, constitute the mechanism usually employed for fund augmentation; by definition, training taxes are compulsory, though in practice tax evasion may be an option where collection mechanisms are weak. This is the case with payroll levies in Tanzania and Zimbabwe. Thus compulsion is a strong element in policies aimed at fund augmentation. In some instances, attempts at resource augmentation have resulted from government pressure, direct or indirect, rather than compulsion. For example, under the former industrial training board system in South Africa, the lack of government measures to support enterprise training led to voluntary attempts at funding augmentation at the sectoral level via levies; these voluntary methods were less than successful.

Both compulsion and pressure modes figure strongly in policies aimed at greater cost sharing. We have noted that, in many cases, the major form of cost recovery is through centrally imposed institutional training fees. Alternatively, pressures from tight institutional budgets (cutting or containing present levels of support) may lead training providers to seek sources of additional income generation through raising training fees. Incentives, such as institutional retention of generated fee income, may act as a trigger leading to greater cost recovery but these effects are not seen to be strong. Usually, compulsion is not an element of policies aimed at the generation of income by training institutions. But as with cost sharing, pressures from constrained institutional budgets lead to income generation. Incentives (such as retaining generated income) can play a

role in encouraging institution to augment income, but not a strong one.

Finally, private sector training development may be responsive to government policies. In particular, government subsidies for private training institutions (albeit set at a lower level than support for public training institutions) are likely to offer strong incentives for private sector training development. But of no less importance is the role of government as a facilitator: to ensure that the institutional environment is conducive to private sector growth.

**Table 7.2
Funding Diversification: The Role of Government Policy**

Intervention Mode	Method of Funding Diversification			
	Fund augmentation	Cost sharing	Income generation	Private training institutions
Compulsion	Strong	Strong		
Pressure	<i>Weak.</i>	Strong	Strong	
Incentives		<i>Weak</i>	<i>Weak</i>	Strong
Facilitation				Strong

Note: a blank indicates 'not applicable' or 'of marginal importance'

7.8 Responding to Budgetary Pressure: Institutional Income in Tanzania

We have noted in Section 5.4.1 that the Tanzanian training authority, VETA, has neglected the development of private training capacity; however, it has achieved more success in cost sharing and income generation.

VETA owns and funds the network of public training centers, mainly through a two percent payroll levy. This network consists of ten Regional Vocational Training and Service Centers (RVTSCs) which service the overall training needs of the regions, seven smaller vocational training centers (VTCs) and the Morogoro Vocational Teachers Training College (MVTTC). The annual budget for each VETA-owned institution includes two income heads, for 'School Fees' and for 'Other Income Generation', respectively. The school fees category comprises mainly fees for attending training courses, but also other items such as trade testing and application fees. Other Income includes rental income (from hiring out of facilities) and generated income from student projects and training with production.

Each institution is expected to generate the sums designated under these two budget heads. If these sums are not forthcoming, the institution is not given compensating allocations by VETA and institutions will need to accommodate to the shortfall by reduced expenditures. Budgeted self-sufficiency rates vary across institutions; in 2000 it was set at 40 percent (of budgeted recurrent expenditure) for MVTTC and ranged from 11–39 percent for RVTSCs and from 7–22 percent for VTCs. Overall, income from these two sources constituted 27 percent of budgeted institutional income in 2000; 15 percent from school fees and 12 percent from other income generation. This is up from about a fifth in 1999; indeed, it is understood that it is VETA policy to raise the self-sufficiency rate to 40 percent over the medium term.

The system exerts indirect pressure on institutions to ensure that budgeted incomes from outside sources are, indeed, collected. However, scope for institutional initiative varies by type of income source. While most school fees are set centrally by VETA and are standard, as is often the case in other countries, there is still scope for raising total fee income by increasing trainee enrollments. Thus in 1999, some centers raised school fee income though an increase in enrollment due to the introduction of double shifts. Fees for short courses are negotiable locally, as are the various Other Income categories. It would seem that, overall, the system is working; the budget statement for 2000 reports that, overall, income received from these two categories was in close conformity with budgeted income. However, outcome variation is likely across institutions.

Discussions are currently underway on plans for the decentralization of the VETA framework, envisaging moves towards considerable local autonomy, especially for the RVTSCs; hopefully, this will include also greater institutional autonomy in the setting of user fees.

7.9 Lessons for Policy

In this chapter, four options have been presented for the diversification of funding to public sector institutional training, with a view to reducing the financing burden falling on public budgets. We noted that these options operate in different ways (Chart 7.1): three act directly in bringing in additional revenues to the training sector while the fourth affects training budgets only indirectly. Thus, additions to total funding available for allocation to training providers may be secured through the levying of payroll taxes. Again, training institutions may augment public budgetary allocations through cost sharing (in particular through introducing or raising course fees) and through income generation (largely from combining production with training). And, finally, encouragement may be given to the development of private training institutions.

These diversification options are not alternatives; all four avenues may be explored simultaneously. However, whether or not to do so, remains a policy issue; this will depend on a number of factors including the feasible scope of the intervention and on the balance between the advantages and weakness of the approach, in each case. We now turn to a consideration of these issues in relation to a major variant of each of the four options.

7.9.1 Scope for Funding Diversification

The dominant tool for fund augmentation is the training levy. The scope for levying payroll taxes is well established by international experience in SSA countries and elsewhere: almost all countries that have introduced payroll levies have set the levy rate in the range of one to two percent of company payroll bills, the majority at the lower end of the range.

There is considerably less conformity of practice in relation to raising tuition fees as a measure for increased cost sharing or of income generation by training institutions from production. This should not occasion surprise. The feasibility for tuition fee setting (in relation to unit costs of training) is a compound of many and diverse factors; these will vary from place to place. They include: type and costs of training, the price elasticity of trainee demand for different training courses, political constraints, policies for equality of opportunity, and the presence of student aid to assist disadvantaged students unable to meet the new, augmented fee levels.

In similar fashion, the scope for generating income from production by training institutions will also depend on numerous local factors, including the nature of the product, local demand conditions and potential market competition. Thus it is not possible to be prescriptive in relation to the scope for generating revenues from tuition fees or for augmenting income through production combined with training. These are issues that will need to be settled on a case-by-case basis, in the light of local conditions and possibilities.

7.9.2 Diversification Mechanisms: Strengths and Weaknesses

A listing of the major advantages and risks of the four options is set out in Table 7.3.

Table 7.3
Mechanisms for Funding Diversification: Advantages and Risks

Mechanism for funding diversification	Leading policy variant	Income accrues to:	Advantages	Risks
Fund Augmentation:	Training levies	Public sector/ training funds	Diversifies the revenue base for financing training, by mobilizing additional revenues	See listing in Table 6.3
			Can provide a stable and protected source of funding for national training provision	
Cost Sharing:	Raising tuition fees	Training institutions	Will make training more cost-effective as training institutions vie to attract trainees	Imposes hardship on disadvantaged students, depending on scope of

				scholarship policy
			Training will become more demand oriented	Income may not remain with the training institution
Income Generation:	Income from production	Training institutions	May lead to training outcomes more closely geared to the needs of the market.	Neglect of the training function, lowering the quality and quantity of training
				Too many resources may go to production rather than training
				Income may not remain with the training institution
Private Training Provision	---	No income generation –budgetary savings to public sector/ training funds	Expansion of the national training system can be achieved– and without commitments of public funds.	The concentration of private providers on low cost, high demand courses, may leave public sector institutions with the more costly, technical courses and limited possibilities for across–course subsidization

8 Funding Distribution: Transfers to Training Institutions

This chapter is concerned with the criteria to be used for institutional funding. For simplicity of exposition, we present the discussion in terms of the institutional allocation of funding by government. It should be noted however that the argument is equally applicable to situations where a training fund (financed by government, training levies, or both) replaces the government as the body responsible for financing training institutions.

We have noted that the allocation amongst training providers of the total government training budget emerges as a major component of the financing system in all three training market scenarios discussed above, not the least in conventional training markets (as shown in Chart 4.1 above). In very many countries, a clearly formulated, transparent disbursement policy is lacking. Yet the mechanism through which government transfers funds to training institutions is likely to have an important effect on the way in which this funding is used and on institutional behavior more generally. In particular, we shall argue that inherent shortcomings in the transfer mechanisms used may promote low internal efficiency of training institutions and a strengthening of supply–driven training provision.

8.1 Direct Allocation Mechanisms

The methods currently in use for the *direct* allocation of state funding to public training institutions vary widely across SSA countries; we consider *indirect*, student–based, funding subsequently. These direct funding transfer methods may be grouped under three broad categories (see Ziderman and Albrecht, 1995 for a parallel, but fuller, discussion of institutional funding at the university level). Funding allocation may be based on objective criteria relating to the internal workings of the training institutions: related either to the *outputs* of

the training institution or to its *inputs*. More generally, however, governments eschew the use of internally-related objective criteria (inputs or outputs); we group these other methods together as *ad hoc funding*.

8.1.1 Ad Hoc Funding

We include under *ad hoc* funding such wide-spread practices as incremental funding, where institutional allocations are based on those of the previous year, often augmented by across-the-board incremental budgetary increases or perhaps according to political influence, interest group pressure or the negotiating skills of the institutional actors. Such *ad hoc* systems of allocation, rooted as they are in the *status quo*, are unlikely to facilitate internal efficiency or market-oriented dynamism. Indeed, a major defect of *ad hoc* funding is that it provides no incentive for institutional efficiency. Clearly, if funding is unrelated to the internal activities of the training provider, there are no incentives built into the funding system to promote greater efficiency – and the opposite generally is the result. The other major shortcoming of *ad hoc* funding – one that is shared, we shall argue, with input and output-based funding – is that it does nothing to encourage training providers to be adaptive to labor market needs; training provision remains static and supply-driven.

Ad hoc funding in Zambia: The 23 Trades Training Institutes in Zambia are funded by the Ministry of Science, Technology and Vocational Training (MSTVT), through largely *ad hoc* funding methods. Institutes present annual budget requests to the MSTVT. Initial institutional allocations are based on the previous year budgetary allocation (with an allowance for inflation) but subsequently adjusted downwards to reflect the lower total budgetary allocation approved by the Ministry of Finance. The upshot is that salary allocations for permanent staff continue to absorb almost all of the budget for recurrent expenditures, leaving little available for materials, supplies and maintenance. An independent (restricted circulation) review of training finance in Zambia concluded recently that this funding approach has encouraged complacency amongst training providers since funding is secured regardless of performance and little attention is accorded to training quality or provision relevance.

8.1.2 Input-Based Funding

A more objective alternative is to fund institutions on the basis of the estimated costs of inputs required for training provision. The simplest, but least satisfactory, form of input funding is to base allocations on itemized budgets for future years, submitted by training institutions. Since overall budget allocation for each institution is based on approval of individual expenditure items, this form of funding leads to inflexible line-item budgeting, restricting the use of funding only for approved purposes.

A more flexible form of input funding derives institutional allocations from formulas, typically based on trainee enrollments or number of classes. The most common approach is to multiply enrollments by a parameter of unit costs; formulas may be enriched to take account of the differing cost of various training courses. Governments may use input formulas as a form of indirect control over enrollment patterns, by employing differential weightings (or coefficients) based on course offering or student background. In the latter case, the funding formula can facilitate the achievement of policy goals by encouraging training institutions to seek out, and admit, disadvantaged youngsters, the unemployed and minority groups. In linking funding to the cost of training activities, input funding secures a far greater level of accountability than is forthcoming under *ad hoc* allocation.

However two inherent problems are associated with input funding. First, there is little incentive for efficiency. Indeed, funding formulas based on average costs provide incentives for institutional expansion, perhaps regardless of trainee suitability; nor do they offer quality assurance, either in terms of the quality of the training offered or its job-relevance. Secondly, because input budgeting promotes a training environment that is divorced from employment needs and the job market, it may lead to a training system that is out of kilter with the realities of the labor market.

8.1.3 Output-Based Funding

The concepts of 'payment by results' and rewarding performance underlie output-based methods of funding. Output-related funding provides financial incentives to training institutions by rewarding them for meeting certain predetermined levels of training delivery (Felstead 1998); training institutions not achieving these predefined outputs are penalized. Outputs may be measured in absolute terms (often defined as the number of course completions) but may also relate to the speed with which outputs are produced (to minimize cost-enhancing repetition).

The most important benefit to be gained from adopting output based funding is enhanced efficiency of the training process. Since a training institution's budget is linked to the achievement of particular outputs, an incentive is present for training institutions to change and improve various aspects of their training policies and practice, in order to increase their training performance and, hence, funding.

Output v. outcomes: Output formula funding as discussed thus far may be appropriate for addressing problems of internal efficiency of training institutions. But it is unlikely to provide a good proxy measure of the labor market prospects of trainees nor does it lead to a better matching of training activities with the needs of the market. In sum, it does not result in a greater demand-driven orientation of training. In this regard, a distinction between two types of performance-related budgeting should be drawn; this distinction is not usually emphasized in the literature. The type of output-based funding considered thus far relates to process, to the internal training activities of the training provider. This may be contrasted with training outcomes, on how well the training programs impact with the labor market. Outcomes may be defined in terms of the success of the training provider in meeting labor market needs; this can be measured by the percentage of course completers who are placed in jobs and by the speed with which they are absorbed into employment.

Creaming and dredging: Output/outcome measures may lead to 'creaming', a process whereby training providers screen out less promising candidates in order to maximize measured output performance. Creaming is likely to result in the exclusion of the poor, unemployed youth, ethnic minorities and other disadvantaged groups – the very population segments at which the training program may be aimed. This tendency may be countered in a number of ways. A greater weight could be given in the reward structure to outputs drawn from these disadvantaged populations. For programs aimed at special groups, the government could set upper limits on course eligibility, a practice known as 'dredging' (Felstead 1998).

Initial placement v. sustained employment: Inevitably, outcomes will be measured in terms of success at initial placement of trainees; this may not correspond to the achievement of sustained employment over the longer term, the ultimate goal of training programs. Indeed, providers thus may be encouraged to narrow training content and concentrate on meeting short term market needs rather than designing more flexible training that is better suited to changing labor market needs (Felstead 1998). It is possible to measure these longer term outcomes through well designed follow-up studies; indeed, outcome studies of this type rightly should constitute an integral part of evaluation and feedback in all training programs, though the capacity for conducting these studies may not be in place in many SSA countries. However, it may be less than practicable to base payment on measured long-term employment effects, given the additional uncertainties and payment delays this would introduce.

8.1.4 Composite Formula Funding

In general, the implementation of formula funding methods will require a framework that strikes a balance between the individual institutional response to efficiency incentives (i.e. to adjustments to its funding) and the need for annual funding stability. For example, output-oriented funding schemes, while leading to better performance, may result in funding instability, as institutional income will depend on outcomes, in turn subject to the vagaries of economic activity. If institutional funding is based solely on performance, year-to-year variations in funding may lead to cash-flow problems, thus complicating (even disrupting) the ongoing training process. And funding uncertainty will discourage institutional initiative and change. Thus output-based funding is unlikely to be successful if used as the sole criterion for funding.

Indeed, formula funding is likely to be most efficacious where broadened to include a number of constituent elements. This composite formula funding could include such elements as institutional inputs, outputs, desired labor market outcomes and the enrollment of special groups. Individual weightings would be assigned to each element. Weightings would reflect the tradeoff adopted between the need for efficiency incentives and stability; they would conform to the relative importance of each element in terms of the overall objectives of the training program in question. The input element (probably total enrollments) would offer greater institutional funding stability, while the output element would provide incentives for internal efficiency of training institutions. The element reflecting labor market outcomes (say job placement) would offer rewards for external efficiency of the training and bring the training system closer to market needs. Elements relating to the enrollment of such special groups as the unemployed, poor and disadvantaged youth would facilitate the achievement of social goals; the inclusion of a higher weighting factor for enrollment of lower ability trainees would help to offset tendencies towards creaming.

8.1.5 Competitive Tendering: Unifying Training Markets

Finally, we need to draw a distinction between the funding of publicly supported training institutions (as discussed thus far) and the method to be adopted for financing training for more specific target groups, such as those with special needs or from the informal sector. In the latter case, it is common for the government (or a training fund) to provide special funding to public institutions to put on the required training courses, perhaps employing allocation methods of the type discussed above. Increasingly, this funding is made available on the basis of training contracts, between the funding body and the training institution, specifying the range of training services to be provided and, perhaps, measures of success against which final payments are made. However, this approach may lead to irregularities in the allocation of contracts; it provides few pressures on the training system to operate efficiently, at low costs (bringing savings on national training budgets) and usually operates as a 'closed shop' largely denying entry to private providers. A system of competitive bidding can offer a framework for avoiding these shortcomings and for providing for a more cost-conscious, competitive environment in training provision, in which private providers can compete on equal terms with public training institutions. We discuss some SSA cases, below.

*Training contracts for informal sector training – Cote d'Ivoire.*⁷ In recent years the payroll levy financed Vocational Development Training Fund in Cote d'Ivoire (FDFP) has extended its areas of training support to include training for small firms and the informal sector. The FDFP finances its training programs for target groups under this program through the award of training contracts made to pre-qualified training providers (from the public and private sector) on the basis of competitive bids. The process of pre-qualification includes field visits of FDFP staff to training provider applicants and assessment of training capabilities according to particular fields of competence; pre-qualified training providers constitute the pool from which competitive bids are drawn. A proposed training program is sent to three to six pre-qualified training providers in the relevant field of competence; a contract is awarded on the basis of the best bid received.

In the past, the FDFP had not employed a process of competition amongst training providers in the award of contracts and collusion and irregularities had been rife. The present system of competitive tendering has led to lower unit training costs, compared both with earlier years and with other regular programs supported by the Fund. One notable outcome has been the success of private training providers in gaining training contracts. The fear that publicly subsidized training institutions would benefit from an unfair price advantage over private providers has proved to be unfounded; public providers receive only about a quarter of training contracts. There is evidence that the competitive process has been successful in infusing a more entrepreneurial approach amongst management in public, as well as private, training institutions.

Funding public training delivery – South Africa: Under new financing arrangements currently being put in place in South Africa, budgetary allocations would continue to fund training programs for special groups, including the unemployed and youth, as well as pre-employment public sector training. Proposals for the disbursement of public funding for training programs aimed at target groups envisage the removal of protection from public training providers and the introduction of performance-related funding criteria. A new system of competitive tendering for long-term training contracts will be adopted. These measures would put an end to the privileged position of such public sector providers as the Regional Training Centers, in relation to existing and emerging private sector institutions. The system aims at encouraging competition between institutional training providers, both public and private, and would enhance providers' responsiveness to the performance criteria against which public funds are to be allocated.

8.2 Indirect Allocation: Trainee-Based Funding

While it is current practice in SSA countries for the state to support public training by direct transfer of funds to training institutions (usually through *ad hoc* methods), in principle an alternative, indirect route is available through subsidies to students/trainees. In earlier chapters we have emphasized the advantages of a labor market oriented, demand-driven public training system; one approach towards moving the training system in this direction is through a student-responsive institutional training system with greater cost recovery through higher, more realistic training fees (in concert perhaps with trainee loans). But this may not be socially acceptable or politically practicable; indeed, when labor markets are distorted resulting in narrow skill differentials and low returns to private investments in training, it may not be feasible either (see Middleton, Ziderman and Adams 1993). Moreover, student loans have not proved to be a suitable vehicle in SSA countries for facilitating substantial cost recovery (Section 7.4.2). Thus government subsidy remains on the agenda.

8.2.1 Vouchers

In principle, it is possible to achieve many of the benefits of a trainee-responsive system, without moving strongly away from state subsidies and towards greater cost recovery. Institutional training subsidies could be maintained at present (or other suitable levels) but channeled through the trainees in terms of training vouchers (or perhaps subsidized loans). Thus subsidization could take one of two paths (given the level of public subsidy of institutional training that is deemed appropriate); subsidies could be paid directly to the institutions themselves, as is current practice, or via the trainees. The alternative funding routes are shown in Chart 8.1 (in practice, both paths are likely to be used as complementary approaches). The right-hand side of the chart illustrates direct institutional allocations from government (or a training fund); training is free or offered at nominal fees. Alternatively, the subsidy could be made via the trainees themselves, as shown in the left-hand side of the chart; students would meet tuition fees charged by training institutions, wholly (or in part) through vouchers of entitlement to training courses; we refer to this as trainee-based funding.

Many advantages are claimed for a system of subsidy through student-based vouchers. A central motivation for trainee-based funding is to promote competition amongst training providers as they compete for trainee enrollments, in terms of type and quality of program and in tuition fee level. Vouchers could be used at private training institutions too, thus increasing market competition and widening trainee choice. The system would lead to greater institutional efficiency and quality and training provision that is closer to market needs.

In some respects, student-based funding will appear to be similar to an input funding formula based on the number of students enrolled. Indeed, from a purely accounting point of view there may be little difference between whether funds are transferred directly to institutions (on the basis of enrollments) or via a voucher mechanism. However, a vital distinction should be made between the two, in terms of the context within which trainees and institutions make their decisions. A trainee-based funding system operates within an environment that offers real choices to trainees in terms type, quality and price of training and, in parallel, where competition between public and private training providers is the norm. Direct funding functions within an environment that is more constricted, in which institutions have less scope to differentiate their offerings and to use resources as they see fit, and students have far more limited choices. As these restrictions are loosened, the system moves from direct to, essentially, indirect funding. What we have called trainee-based funding, in effect, represents a suitably reformed input-based funding system, in which competition and student choice become the fulcrum of the funding system.

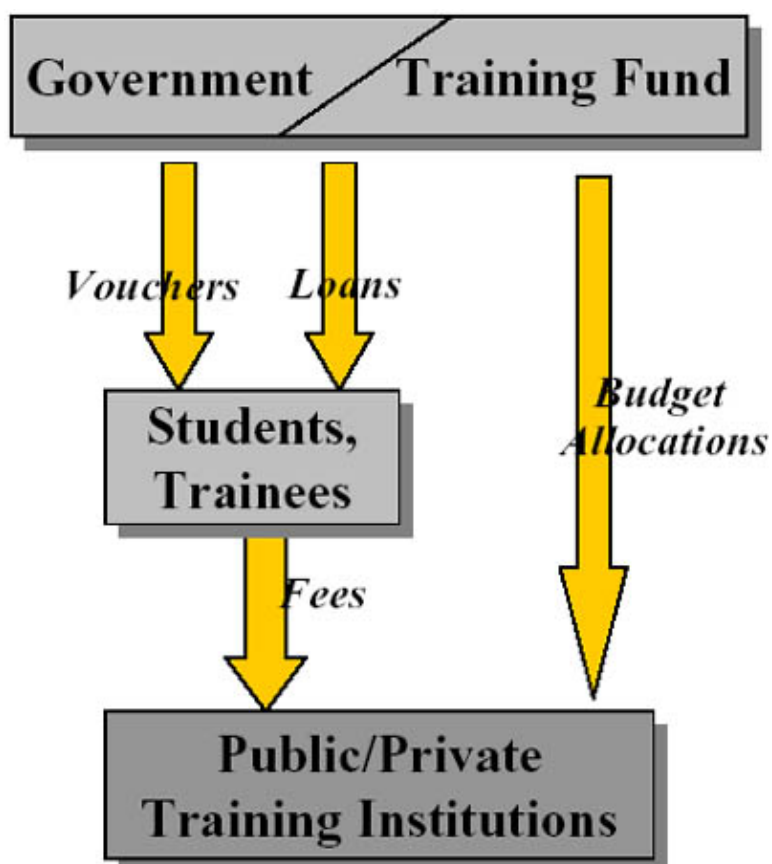


Chart 8.1 Alternative Pathways for Funding Institutional Training

Movement to general student-based funding remains a long way in the future. However, it has a more immediate role to play in more specific training contexts. Indeed, several countries are currently using

vouchers, in largely experimental programs, as a mechanism for the funding of training for the informal sector, with the longer term aim of building up demand-driven training markets for informal sector training. The best known example is the voucher program in Kenya providing support for micro and small enterprises, but there are others, including the Mauritius scheme and the flawed intake voucher scheme in Ghana. We shall consider these further in Chapter 10, dealing with the informal sector.

8.3 Policy Reform

We have noted that *ad hoc* institutional funding remains the norm in the region however; it is widely recognized that such, largely arbitrary, funding allocation methods may encourage internal inefficiencies and strengthen tendencies towards supply-driven training. Yet, unlike the case of other desirable training finance reforms, moves towards more objective criteria seem well within the grasp of the governments in many countries and there has been some promising experimentation with these methods in current training institution reform in the region. Barriers to progress may stem more from institutional resistance, opposition of vested interests and the slowness of higher education institutions, which would be expected to lead the way here, to move in this direction. But change could well be on the horizon in countries formulating a broader package of institutional reform; objective funding criteria might then constitute part of a more general reform of institutional funding, which would include reduced public funding overall (replaced by cost recovery and income generation), decentralization and enhanced institutional autonomy and a greater use of contact funding.

9 Enhancing Enterprise Training

Our discussion in Chapter 3 pointed to the tendency for firms to under train; we discussed some of the underlining reasons for this. We noted that a legitimate response was the offer of training incentives for firms, in the form of the direct subsidy of enterprise training by the government; direct training subsidies could be provided also as part of a levy-grant system. Or indirect subsidies could be offered through concessions on company tax obligations for firms that train. In this chapter we discuss these different forms of incentives for company training and consider how far they may be successful in improving training outcomes of enterprises.

9.1 Direct Training Subsidies

9.1.1 Government Grants v. Levy-grant Schemes

Some countries offer direct subsidies (out of public funds) to encourage company training. In what ways does this differ from cost reimbursement, as part of a levy-grant scheme? In Section 7.3.1 we noted that, from the funding side, training levies are beneficial in easing the financing burden falling on government. On the side of training incentives, also, levy-grant arrangements are likely to be far more efficacious than government-funded training subsidies. With a subsidy scheme, here as in other areas of subsidy, incentives may be indirect and insufficiently focused, failing to catch the attention of senior management. Perhaps too much reliance is placed on the initiative of the individual firms involved- in knowing that the subsidy scheme exists and that the firm is eligible for subsidy and in overcoming company lethargy and committing to the burdensome process of involvement in the scheme. But in the case of levy-grant schemes, 'involvement' is assured automatically by the compulsory payment of the levy; anecdotal evidence suggests that senior company finance officers may tend to exert pressure on the training function to ensure that "we get back the levy", through appropriate training provision.

From the viewpoint of the levy-grant scheme (as with government training subsidies), the grant encourages training; but from the firm's standpoint in levy-grant schemes, training recoups the levy! Thus while there may be a dichotomy between the motivations of the scheme as a whole and that of individual firms, the same end result is achieved: more enterprise training. Moreover, there are likely to be positive longer-term effects. The experience of the former UK industrial training levy-grant system was that, in time, the process did exert the beneficial effect of increasing training consciousness in the firm; the training function, as a generator of income, moves more towards center stage in the firm's operations.

Finally, we shall argue that one advantage of a well developed levy-grant scheme over direct government subsidies is that the former is better positioned to adopt a structured, comprehensive approach to training, rather than a more *ad hoc* one. The central lacunae in training under-provision is not only that amount of training provided is too low, but also that it is often piecemeal and not sufficiently well integrated.

9.1.2 Efficacy of Direct Training Subsidies

A question often posed when appraising the efficacy of training incentives through grants (from government subsidies or a levy–grant scheme) is whether they result in more training. But in practice, this question may prove to be rather an empty one. There are several reasons for this.

First, statistical evidence of additional training may not indicate that the scheme is successful. Unlike the case of revenue generating levies, where it is readily observed whether public training institutions are training more, the identification of additional enterprise training that genuinely results from training grants, is fraught with difficulties. Dougherty and Tan (1991 and 1997) refer to the 'repackaging effect', where existing training provision, that does not readily fall within the remit of the incentive scheme, is adapted and repackaged so as to appear to comply with the eligibility requirements for grants. And where there is an increase in the types of training that the scheme sets out to encourage, it may be unclear whether this is due to the scheme itself or whether it would have been forthcoming anyway. Firms that have consistently adopted positive policies towards training provision in the past will receive windfall benefits; this may represent a misallocation of funds unless cost redistribution is an objective of the incentive scheme.

Second, incentive schemes may lead to distortions in terms of the type of training provided. It is to be expected that the more extensive are the incentives offered by the scheme, the greater would be the enterprise response in additional training. But by the same token, generous training incentives may make many types of eligible training now profitable to the firm, even though the firms' needs for these training skills may be doubtful. We return to this theme below.

For reasons such as these, we need to view with some caution claims of success made for individual incentives schemes, based on increased numbers of workers trained. Little careful research seems to be available on this issue. Dougherty and Tan (1991) define the lacunae in this way: they argue that we lack studies that "document comprehensively and in detail the training provided by a sample of firms before the introduction of the scheme and afterwards – in other words, what is needed is an in–depth micro approach, rather than the aggregate approach adopted in the literature to date."

9.2 Levy–Grant Schemes

The discussion on payroll levies in Chapter 6 concentrated on the levying side of these schemes; we now focus on aspects of outcomes of the 'grant', in levy–grant schemes.

9.2.1 Training Off or On–the–Job?

Enterprise training can take on many forms (Chapter 2). Training may be provided in the form of apprenticeship (often divided between training on–the–job and the attendance at courses provided at outside training institution). It may be given wholly on–the–job as initial or continuing formal training, or training may be less formal and ad hoc, though not necessarily less important to the skills development of the firm. It may be provided off–the–job, in the form of formal courses, for workers, management or professionals at specialized training institutions. What forms of training should a levy–grant scheme support?

There is a dilemma here. It may be important to encourage certain forms of on–the–job training but these may be expensive to monitor for quality, and abuse may be difficult to detect. Other forms of training, such as those for professional qualification at recognized external institutions may more readily be subject to surveillance but are not always of highest priority for the firm. This may explain the focus of a number of levy grant schemes. Apart from apprenticeship training, which is largely in decline, most training that is recognized for cost reimbursement in the Zimbabwe scheme, is training for upgrading or professional qualifications at external institutions; more hands–on, practical training does not receive sizeable support. Similar considerations seem to apply to the Kenyan scheme.

9.2.2 Systems Approach v. Piecemeal Reimbursement

A related issue is the breadth of the overall program of training supported by a levy–grant scheme within a firm and its sustainability over the longer term. We may recognize two contrasting approaches here. One – we may label this as the 'external approach' – is typified in the Zimbabwe scheme. Here, a detailed list is produced of approved forms of training and courses that are eligible for rebates; firms are then invited to apply for cost reimbursement for those forms of (mainly external) training it has sponsored and which match items on the approved list. The latest ZIMDEF list dates back to 1993 and is generally regarded as outdated; it is

currently being revised. But this approach, while offering rebates to firms for certain forms of training and probably encouraging firms to train more (in designated eligible areas) is unlikely to have more than a limited, short-term impact on skills development in the firm and may indeed distort the balance of forms of training provision within the enterprise. This is because it gives recognition, and financial support, to more standard forms of training – usually provided externally to the firm – that are more readily recognized and easily monitored (and thus countering potential financial abuse) rather than to supporting more needed forms of training, varying across firms and often less formal or standardized, which is lacking in individual enterprises.

An alternative, 'systems' approach – elements of which are found in the Core d'Ivoire, Nigerian and the newly developing South African schemes – takes a broader view. In Cote d'Ivoire levy exemption and cost reimbursement are contingent on the preparation, and approval by the Fund, of a company training plan. In the Nigerian case, grant payment is conditional on the firm adopting a systematic approach to training based on given criteria; thus firms are encouraged to begin to think systematically through preparing a training program, defined in terms of their real skill needs, rather than applying for rebates on a purely *ad hoc*, short term basis. This more progressive approach is being developed within the framework of new funding arrangements being put in place in South Africa; to these we now turn

Disbursement arrangements in South Africa: In South Africa, 80 percent of the proceeds of the new skills development levy passed is on to each Sector Education and Training Authority (SETA) in accordance with levy sums paid by employers in each sector; the remainder goes to the National Skills Fund. Use of moneys received by the SETAs are narrowly prescribed in the annual funding regulations issued by the Department of Labour. The regulations for the first year of operation of the scheme (financial year 2000/2001) place a cap on SETA administration and operation cost and exceptional set-up costs of 30 percent of levy proceeds (i.e. 24 percent of SETA receipts). More relevant to our present discussion – each SETA is required to distribute back to employers at least 50 percent of levy proceeds as grants.

These grants are of two types: rebates to the employer, based on the levy paid and discretionary cash grants. Rebates take the following form: employers may receive back 15 percent of the levy for the appointment of a skills development facilitator, 10 percent for the preparation of a workplace skills plan and a further 20 percent for its implementation. Thus the emphasis in this first year of operation of the scheme is on planning and developing structured training, in line with identified company needs. Companies are required to carry out a comprehensive training skill needs assessment, by identifying their strategic development priorities and mapping in the education and training required to achieve them. Thus, eligible training for rebate is not decided by a central, outside body – as in the external approach mentioned above – but evolves internally in each case through an identification of the particular skill development need of individual firms.

SETAs are required to use at least five percent of levy income for grants to employers for special skill initiatives in the sector; these grants are not dependant on an employer's levy contribution and individual employers may receive a discretionary grant in excess of five percent of levy payment.

9.3 Indirect Subsidies: Company Tax Concessions

In most countries, training expenses incurred by companies are tax deductible, as are expenditures on capital assets. The tax treatment of training expenditures (a form of human capital investment) is typically more favorable than that of machinery and equipment (Dougherty and Tan 1991). Training expenses are tax deductible immediately, whereas physical assets are tax deductible only in installments, over a number of years, through depreciation allowances. However, a training incentive may be given in the form of further tax concessions for company training expenditures, in addition to the usual deduction of training expenses for tax purposes: we refer to these as 'company tax concessions.'

9.3.1 SSA Experience With Tax Concessions

Following Gasskov (1994), most of the literature discussion of the use of company tax credits as an incentive device for enterprise training is concerned with two well-known Latin American examples: the generally successful and extant scheme in Chile and the failed (and phased out) Brazilian scheme. However, there are number of (lesser-known) SSA examples of interest, but all generally unsuccessful.

South Africa: The (now defunct) industrial training board system in South Africa was preceded by a company tax concession scheme, established under legislation in the 1970s. The scheme allowed for the deduction of 200 percent of training expenditures (reduced to 150 percent in 1984), thus effectively reducing training costs of profitable firms by half (at a corporation tax rate of 50 percent). The scheme was faulted by "gross abuse"

of the concession by employers and difficulties in policing claims. Moreover, employer uptake was very low; well under one percent of firms in the country claimed these tax concessions for in-service training (National Training Board, 1986). It was replaced for a limited period by a system of cash grants, provided to the first industrial training boards by the Department of Labour.

Botswana: In the Botswana scheme, employers are also able to deduct 200 percent of training expenditures from the corporate income tax, effectively reimbursing 70 percent of training costs (Franz 2000). The scheme is virtually unused; employers are largely unaware of the scheme and procedures are highly complex. Franz (2000) attributes the ineffectiveness of the scheme largely to the fact that the institution granting tax concessions (the Finance Ministry) is not technically competent to make decisions on concession eligibility, a problem shared with the South African scheme. Decisions on eligibility for tax deductions was made by the trade testing institution (MTTC) under the Labour Ministry. "In theory, an employer would need to approach MTTC for approval of its training, and afterwards submit this approval together with the complicated cost statements to the Ministry of Finance.....It is hardly surprising that only a handful of companies had followed this cumbersome procedure" (Franz 2000)

Mauritius: The Mauritius scheme is unusual in this continent in that it operates in tandem with a levy grant scheme. The presence of two schemes together is not unique – Brazil, for example, also operated both schemes in parallel, though unsuccessfully. What is unusual is the close integration of the two schemes in Mauritius. The combination of tax incentives and levy-grants, under which firms in principle may receive reimbursement of up to 75 percent of training expenditures, has resulted in a somewhat complicated training cost reimbursement formula. Firms can receive various levels of tax relief according to the rate of corporate tax that applies to them; the grant from the training fund could bring total relief up to 75 percent of training costs. Thus firms not liable to corporate tax may receive a reimbursement grant of up to 75 percent of training cost; a firm with a 15 percent tax rate can receive up to 60 percent rebate and deduct an additional 15 percent of training costs from tax obligations. Overall, the administrative and supervisory costs of the scheme are unnecessarily high, it has led to conflict over the interpretation of the rules governing the interrelationship of the two schemes and as a consequence the reimbursement element of the levy-grant scheme has remained small.

9.3.2 Problems with Tax Concession Schemes

The major problems with tax concession schemes are simply stated. A pre-requisite for the introduction of the scheme is a well-developed and broadly-based system of corporate taxation, not usually present in SSA countries. Firms with low profits and perhaps poor training capacity do not benefit and are not encouraged to train. Tax concession schemes only offer benefits to stronger, profitable firms. And unlike levy-grant schemes, it is the government that bears the cost of these schemes in the form of lost tax revenues; in this sense they are akin to direct training subsidies by the government and may be regarded as representing 'subsidies in disguise'.

9.4 Other Measures to Promote Enterprise Training

9.4.1 Apprenticeship Training

Subsidizing apprentice wages: In many countries, apprenticeship training is a key method of skills development for the formal employment sector. Support for apprenticeship training, in the form of subsidizing the wages of apprentices, often constitutes part of a wider regime of government training subsidies or levy-grant schemes, as described above. A particular case can be made for subsidized apprenticeship wages on both equity and efficiency grounds.

The subsidy of apprentice wages may raise the level of remuneration accruing to trainees. Picking up on themes developed in Chapter 3, the equity case relates to giving parity of treatment to apprentices with their peers (including those in vocational schools) who continue on within the (highly subsidized) formal education system. Moving from the viewpoint of the individual apprentice to that of the firm, wage subsidies serve to lower the cost burden of training falling on the firm, in conditions where the costs of apprenticeship training are not passed on fully to the trainee. In calculations of apprenticeship costs in Zimbabwe, Suhr (2000) shows that apprentice wages account for about half of annual gross costs of apprenticeships in the automotive industry. Related to these points, Dougherty and Tan (1991) offer the following efficiency argument for apprenticeship wage subsidies. Subsidized pre-employment training at public institutions competes with apprenticeship training. Yet institutional training may be the less cost-effective training mode; evidence for Zimbabwe is given in Bennell, 1993 (see also Ziderman, 1989). Increasing the proportion of youngsters taking the

apprenticeship route could lead both to a net saving in public funds and more cost-effective skills development.

Apprenticeship wage subsidies may be provided in many different ways. They may be offered for the whole of the apprenticeship period as in the Malawi case (see below). Alternatively, wage subsidies may be confined to the earlier years of apprenticeship only, where the net value of apprenticeship output may be low or negative. Thus in Zimbabwe, apprentice wages are financed by the Zimbabwe Manpower Development Fund for the first two years of the four-year training cycle. Support may be particularly appropriate during periods of instruction, off-the-job, at formal training institutions (where no apprenticeship output is forthcoming).

Apprentice wage subsidies can be a useful tool, positively influencing the quantity of initial training provided by companies; however, for this to be the case, a number of preconditions must be present and various pitfalls avoided. First, employers may exploit the availability of apprentice wage subsidies, to gain access to cheap labor. Second, the elasticity of supply of apprenticeship slots should not be low, in which case the desired supply response of an increased apprenticeship intake will not be forthcoming. And third, the periods spent in apprenticeship training on-the-job must provide genuine training and skills development for the worker, in turn imposing costs on the firm which are offset (in part or full) by the wage subsidy.

Apprentice allowances in Malawi: The levy-financed Industrial Training Fund in Malawi, which focussed mainly on the support of the apprenticeship scheme, is now being replaced by a broader based scheme covering additional levels of training provision and a wider range of skills, beyond apprenticeable trades (Franz, Maleta and Mtambo, 1998). Some three-quarters of levy income was expended on the reimbursement of apprenticeship wages. Apprentice allowances were provided during the four-year apprenticeship period – both during the initial year of fulltime institutional training (paid by the government) and, subsequently, during the three years of indentured training (paid by the firm and reimbursed by the Fund). From the second year on, apprentices received a fixed monthly allowance, including the annual three-month period of block release at training institutions.

9.4.2 Combining the Carrot with "Ear-stroking"

All of the subsidy measures discussed above offer financial incentives to companies to increase their training efforts. But, as with the proverbial case of the stubborn mule, these carrots may not be sufficiently attractive to influence behavior as much as desired. The British economist, the late Sir Dennis Robertson, once referred (in a different context) to the efficacy of "ear-stroking", whereby efforts at persuasion may be employed to complement the offer of incentives. A regime of financial incentives, alone, may be insufficiently strong to achieve the desired increase in enterprise training; the addition of more positive measures may be required. Indeed, financial incentives may prove to be a weak tool for generating more and better training, particularly over the longer term, because they emphasize financial reward and not the importance and value to the firm of the greater training investments themselves. Here, then, lies an important role for the state (or specialized agency) in promoting enterprise training through creating an informed climate of opinion conducive to company training. Measures would include dissemination of information on the benefits to the company of training, the provision of training advisory services, productivity consulting, training assistance and know-how. Experience suggests that these activities are more likely to achieve success where provided by a central specialized training agency or training fund.

9.5 Lessons for Policy

Many countries have policies that subsidize enterprise training, with the objective of enhancing the quantity and quality of company training provision. Three widely considered methods are direct public subsidies, training grants within the context of a levy-grant system and company tax concessions. Company tax concessions have not been widely favored world-wide or in SSA. In this final section, we discuss some problems that are common to all three approaches; we then consider the major advantages and weaknesses of the alternative mechanisms (though on occasion, as in Mauritius, they are used in concert). Finally, some key points in policy design are recorded.

9.5.1 Mechanisms for Encouraging Enterprise Training: Strengths and Limitations

Common weaknesses: The three mechanisms for encouraging enterprise training share a number of weaknesses. Table 9.1 lists these common weaknesses, provides a brief explanation of each, and offers some policy directions for improvement. A central problem in designing policies to counter these weaknesses, is that a given policy measure may lead to an improvement in one weakness but a exasperation

of another. Thus the redesign of training eligibility criteria to avoid training distortions may lead to higher costs of inspection and monitoring, as will improved inspection methods to counter repackaging. A lightening of the administrative requirements on firms may well lead to a increase in company uptake of subsidies but at the expense of data availability for inspection and monitoring. So a careful balance of policy measures will be necessary.

Table 9.1
Weaknesses Common to all Three Mechanisms

Weakness	Explanation	Policy directions
Windfalls	Eligible training may have been provided by the enterprise even in the absence of the incentive scheme	Revoke subsidy, if windfalls are widespread
Training distortions	May bias training towards more formal and externally-provided training, away from informal training on the job	Redesign training eligibility criteria to avoid distortions
Repackaging effect	"The adaptation and documentation of existing training provision to comply with eligibility requirements..." (Dougherty and Tan 1991)	Better inspection methods
High costs of inspection	The central costs of inspection and monitoring, to counter abuse by enterprises, may be high	Raise sanctions and monitor enterprises on a sample basis
Administrative costs on the firm	The cost to the enterprise of establishing eligibility and compliance (including paperwork and record-keeping) may be considerable	Avoid cumbersome administrative procedures / onerous eligibility criteria

Alternative mechanisms: While sharing some common weaknesses, the three mechanisms are not equally efficacious. In Table 9.2, we list some of the major weaknesses and, if any, notable advantages of each approach. A major advantage of levy-grant systems is that they do not draw on public funds, a point of some importance in times of parsimonious government budgets; in addition (as discussed above) they can lead to more systematic, structured enterprise training (though often are not designed to do so). The disadvantages of tax concession schemes militate against their adoption, in other than a very few countries.

Table 9.2
Mechanisms for Encouraging Enterprise Training: Strengths and Weaknesses

Mechanism	Notable Advantages	Weaknesses
General training subsidies (grants)		Cost burden falls on public budgets (increased expenditures)
Levy-grant systems	Costs do not fall on public budgets – they are met by enterprises (or, with incidence shifting, by workers)	
	Can facilitate a more systematic, structured approach to enterprise training	
Company tax concessions		Requires a well-developed and broadly-based system of corporate taxation
		Cost burden of the scheme falls largely on public budgets (reduced revenues)
		Responsiveness of firms often low because few firms earn sufficient profits to benefit from the tax exemptions

10 Financing Informal Sector Training

10.1 The Informal Sector: a Vehicle for Employment Growth

This paper has been largely silent on the question of the financing needs of the self-employed, small firms and micro-enterprises, which we group together to constitute the informal sector. Indeed, this reflects the existing balance of attention between informal and formal sector training in practice; the 'training sector' is oriented dominantly towards the needs of formal sector employment. This is the case whether seen in terms of the type of course offerings in training institutions, in terms of the concerns and budget allocations of national training funds or in the coverage and focus of levy-grant schemes.

Yet this relative 'neglect' of the informal sector is strangely out of kilter with the realities of SSA labor markets. While in Latin America, urban formal employment has grown faster than that in the informal sector in the last two decades, in SE Asia the share of urban informal sector in non-agricultural employment is about 60 percent and growing. In Africa, the employment share of the informal sector is dominant (with a few notable exceptions such as South Africa and Zimbabwe); formal sector wage employment declined from 12 percent of the labor force in the 1980s to 9 percent in the 1990s (Gill, Dar and Fluitman, 1999). Indeed, typically in SSA countries, a growing labor force cannot be absorbed into formal sector employment since government employment growth is no longer feasible and opportunities for increased employment in the private formal sector are very limited. Thus in many countries in the region, substantial employment – and output – growth will be forthcoming in coming decades only in the informal sector;

The importance of the informal sector growth is to be seen not only in economic but also in social terms, since future improvements in the well being of various disadvantaged groups (such as female self-employed and rural populations) are very much contingent upon informal sector growth. Yet skills development for this sector has not kept up with changing needs. Traditional apprenticeship, geared as it often is to transmitting existing practice, may still be appropriate in many settings; but it often results in low productivity and falls short of supplying the broader skills and technical competencies that technological development and industrial change require. In parallel, institutional training is aimed largely at a static formal sector and not well tailored to the needs of informal sector employment and self-employment.

10.2 Developing Informal Sector Training Markets

There is now a voluminous literature on skills development for the informal sector, which both describes critically training within the informal sector (particularly the traditional apprenticeship) and also discusses the mixed record of new training initiatives aimed at, but often external to, the informal sector. A treatment of this material is beyond the scope of this chapter. Here we are concerned with the more limited issue of the financing aspects of these developments.

10.2.1 Departing from Traditional Training

Traditionally, training for the informal sector has been provided largely internally, within the sector itself. Skill acquisition may take many forms, ranging from *ad hoc*, unsystematic learning on the job to more formal apprenticeship arrangements. But in all events, the training is generally received within the context of the day-to-day production activities of the firm itself. The system was self-financing; trainees paid for training in the form of fees or low wages and there was no financing role for government. In many contexts, informal sector training (as is the case for informal sector production) seemed to work well.

But increasingly, these informal sector training markets have been seen as too limited as a means of meeting the broader skill needs associated with industrial development and growth. Apart from 'learning by observing and doing', training is largely confined to initial training; continuing and upgrading training is rarely available. And the system is largely incestuous in terms of skills and 'know-how' imparted. There may be little scope for importing and teaching new methods, technologies, entrepreneurial or management skills, all of which will be increasingly necessary to serve the growing entry flow into self-employment.

10.2.2 Introducing External Training

The need to meet these shortcomings through the provision of appropriate training courses by training providers that are *external* to the firm is clear; these courses would complement internal skills acquisition. Public training institutions, financed through budgetary allocations, have not proved to be very suitable for this

task, focused as they are on the needs of formal sector employment. Hence, the need to build up a training supply response, in terms of specialized training providers geared towards the particular needs of the sector; we discuss some of these efforts subsequently. However, in parallel, demand for these training services may be weak, because relevant information is not widely available and the desire to train may not be strong. And, of course, even if free, training is time-consuming, carrying opportunity costs; hence, these courses are usually heavily subsidized. While cost recovery is usually nominal at best, some county schemes have developed mechanisms (such as vouchers of entitlement) to raise effective demand ('willingness-to-pay') for these services.

We now consider some SSA experiences in fashioning responses to the need for externally-based training for the informal sector.

10.3 Funding Informal Sector Training in SSA

10.3.1 Supply-side Interventions

We note three highly subsidized, supply-side interventions (in Zimbabwe, Tanzania and Madagascar), each operating within a rather differing financing context, though in each case, these projects were funded from donor, rather than domestic, sources.

National training funds, financed by a payroll levy system, are in place in both Zimbabwe and Tanzania (in the former case a levy-grant system, in the latter revenue generation); but in neither case has the fund been centrally concerned, if at all, with the training needs of the informal sector or with its financing. This unfilled role has been taken up, in both cases, by donor agency initiatives in developing, and financing, separate training projects for the informal sector.

Zimbabwe has a large number of institutions which, in various ways, contribute towards the development of small enterprise and informal sector development; these are outlined in Kapoor *et al* (1997). However, there is relatively little attention given to the training needs of the informal sector. A notable exception the Traditional Apprenticeship Programme (TAP), a GTZ financed pilot intervention (now in the replication stage), which aims at enhancing traditional practice in typical informal sector apprenticeships. It does so through providing the apprentice with initial short term technical training and, where necessary, short-term follow up training, which is complementary to the major component of apprenticeship training that is conducted in the workshop. Apprentices, as a prerequisite for entry to the program, must secure apprenticeship attachment; they attend formal courses against a participation fee. A central objective is to provide a route to sustained self-employment in the informal sector. Much emphasis is placed on building up a supply response from existing colleges and training centers; participation as a TAP training provider can be at relatively low cost, because the infrastructure and spare capacity of existing training institutions are effectively utilized, particularly during evenings and vacation periods.

In Tanzania too, GTZ has developed pilot training programs for the informal sector, but in this case it has done so within the framework of, and in cooperation with, the Tanzanian training authority, VETA. However, these programs represent a very small part of VETA's present activities, though they may grow substantially in the future. The program, Integrated Training for Entrepreneurship Promotion (INTEP) aims at providing training opportunities for potential and existing micro and small enterprises (with special attention given to gender balance) in specific fields that local investigation (through VETA regional offices) has shown to offer good business prospects. The pilot training programs were predominantly donor funded, though some financial support was provided by the training levy and VETA facilities were used. As is many training initiatives for the informal sector, while the concept of cost sharing is integral to the INTEP program, in practice participants contributed only very small amounts in fees.

Ongoing efforts in Madagascar to sponsor and develop training for the informal sector are also essentially donor-agency funded. However, they are carried out as a major part of, rather than separate from, the activities of the national training fund (financed mainly by donors, with about a ten percent contribution from government). The National Council of Technical and Vocational Education, which manages the Intervention Fund for Vocational Training, changed its orientation in 1995 (seemingly at the behest of donors) from training support for the formal sector, towards financing projects meeting the needs of small firms and the informal sector, in particular where growth potential was high.

Cross-subsidy – Cote d'Ivoire: The Vocational Training Development Fund (FDFP) in Cote d'Ivoire out-sources training for the informal sector to specialized training providers, to service the needs of defined

target groups, including rural women. The program is of specific interest because training is financed from the proceeds of the training levy, for which small firms are exempt. Thus the program cross-subsidizes informal sector training by using levy funds raised from formal sector employers. The cross-subsidy constitutes about a fifth of the fund's allocations for training. FDFP finances training projects submitted by 'sponsors' (individuals, firms or organizations) for defined target groups, including such as female entrepreneurs; training is provided by pre-approved training institutions (public or private) on the basis of competitive bids. Cost sharing at the outset was minimal; trainees paid no fees but absorbed any indirect costs such as transport. Since 1998, cost recovery increased substantially and trainees contribute 10–15 percent of costs, through fee payment or contributions in kind.

10.3.2 Voucher Schemes

Voucher schemes, operational in a number of SSA countries, aim at building up consumer demand for training courses for the informal sector and at facilitating a competitive response amongst training providers, through the exercising of consumer choice of training institution and course offering. As discussed in Section 8.2.1, voucher schemes typically do not lighten the financing burden falling on the funding body (usually the government); training remains subsidized and cost recovery is not an integral part of the scheme (though it may be present). But vouchers can lead to greater cost-effectiveness of training provision, wider consumer (trainee) choice and an improved demand-orientation of training for the informal sector.

Subsidy schemes – Kenya and Ghana: The largely successful Kenyan scheme is perhaps the best known and most fully developed training voucher scheme operating in SSA. The flawed training voucher scheme that was planned, but never fully implemented in Ghana is instructive in indicating some pitfalls to be avoided in voucher scheme design.

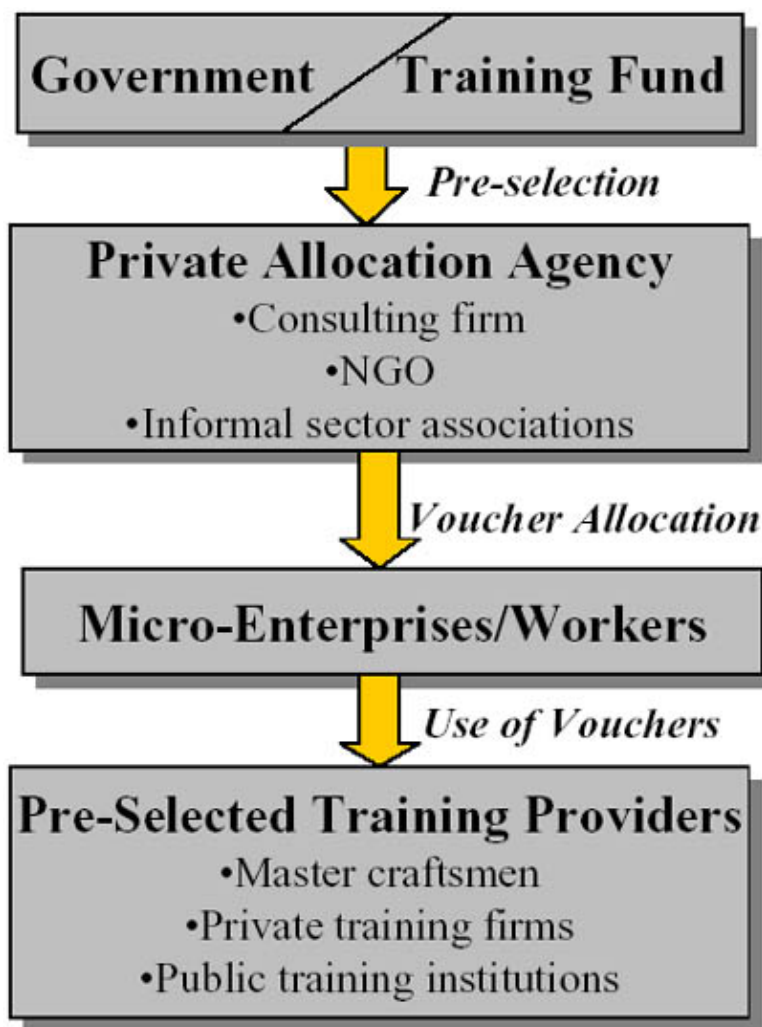


Chart 10.1 Voucher Scheme for Informal Sector Training

Like the supply-side interventions discussed above, the Kenyan scheme is financed mainly by donor funding; it operates outside the framework of the Industrial Training Levy. The highly innovative Jua Kali (micro and small enterprise) voucher program, launched in 1996, is funded by the Micro and Small Enterprise Training

Fund and run by a privately managed Project Coordination Office (PCO) attached in the relevant ministry (in the last five years the PCO has been in five ministries). The scheme is directed towards established small business owners and employees, rather than new entrants, and operates on both the demand and supply side of the training market for informal sector skills. We provide here little more than a synoptic account of the working of the scheme (Chart 10.1); a detailed description is provided in Riley and Steele (2000).

On the supply side, the scheme has similar objects to supply-side schemes discussed above. An important objective of the scheme is to widen the pool of training providers (including master craftsmen) that are capable of catering to the needs of the Jua Kali sector; in the initial stage, a pool of public and private training providers is pre-approved, selected on a competitive basis, in designated skill areas and competencies.

The novel elements of the scheme, however, are found on the demand side. Private allocation agencies are appointed, based on competitive tender, to distribute (and market) training vouchers; the use of these intermediary bodies is regarded as a critical element of the scheme to ensure that vouchers are taken up and that advice and assistance is available to potential trainee applicants. They include private consulting firms, NGOs and Jua Kali associations. Allocation agents receive a fee equal to three percent of the value of vouchers issued. The allocation agent assists applicants in completing voucher applications (which also serve as a screening device to ensure that vouchers are issued to targeted recipients, defined in terms of equity and poverty alleviation); following approval, the agent will issue the voucher to the applicant, on payment of the designated fee (at present ten percent of the voucher value). Voucher recipients enroll in courses offered by pre-approved training providers; on course completion, the allocation agency presents the voucher to the PCO, which authorizes payment to the training provider.

An unplanned, though very positive, outcome was the emergence of a new kind of training provider, well placed to meet market needs for short, practical training, but until now largely unidentified: the skilled master craftsmen. Using vouchers to express their preferences with regard to training providers, Jua Kali workers assigned 85 percent of vouchers to buy the training services of master craft workers, the remainder going to private and public training institutions.

Though sullied somewhat by implementation shortcomings, voucher payment delays and even instances of outright corruption, the demand-led voucher scheme is regarded as mainly successful. It is meeting the central objectives of building the elements of market demand for informal sector specific training and generating a supply-side response in the form of training providers able to meet the very particular needs of informal sector businesses. Over the medium term, however, sustainability will require continued, and substantial, levels of subsidy as willingness to pay for training develops at a slow pace. As the market develops, cost sharing is planned to increase to 50 percent.

In Ghana, efforts to tackle supply and demand side issues within a joint framework were less successful. On the supply side, the development of training programs for the informal sector, with the active involvement of micro-enterprise trade associations, has continued apace. However, the use of 'intake vouchers' for apprenticeship training was planned but never fully implemented.

The planned process comprised the annual distribution of intake vouchers by the National Vocational Council to trade associations, the number of vouchers issued being contingent on the availability of training places in each subject area. The associations would issue vouchers to their member master craftsmen, who in turn would allocate them to relevant workers. The apprentice would enroll at a local, pre-approved private or public training institution, to which entry was restricted to voucher holders. The voucher scheme proved to be unsuccessful and has been replaced by direct trainee recruitment by both trade associations and training institutions. It would appear that the vital intermediary role played by incentive-motivated private allocation agencies in the Kenyan scheme was sorely lacking here. Moreover, the lack of sufficient approved training providers in particular locations largely denied to voucher holders the main benefit of a voucher scheme: consumer choice (and its consequent impact on efficiency, cost and relevancy of training).

Financing through levy-grant – Mauritius: The voucher scheme in Mauritius is unusual in providing a framework within the levy-grant scheme whereby small and micro firms, all subject to the payroll levy, are able to receive training benefits under the scheme. Under-training has been seen as endemic in small firms in Mauritius, the result of both an inadequate training culture in such firms and the difficulties encountered by them in organising training something which the existing training incentives under the levy-grant scheme did little to overcome. Incorporated into the levy-grant arrangements in 1996, the voucher scheme allows for the provision of vouchers to small firms, which may be used to pay (in part or fully) for training received from approved training providers meeting small firm needs. Vouchers are redeemed for payment from the Industrial and Vocational Training Board. The system would lead to an increase in inter-firm equity of treatment under

the levy–grant scheme, lighten the administrative burden that may weigh heavily on small firms in making reimbursement claims and ease their cash flow problems (Franz 2000).

10.4 Policy Dilemmas in Financing Training for the Informal Sector

Throughout SSA countries, considerable population (and labor force) growth, combined with minimal employment increases envisaged for the combined public and formal private sectors, will place an increasing absorption burden on the informal sector. While traditional informal sector training markets, characterized by non–structured within–firm skills acquisition, has served the sector well in many locations and business environments (and frequently continue to do so), the system is proving too narrow to cope with the increasing challenges emanating from technical change, skills enhancement and the widening of geographical markets. Public institutional training has not been able to adapt to the particular skill needs of the informal sector. Thus an increasingly central role for specialized training providers (external to the firm) is now seen, both for entry training into new skill areas and developing markets as well as for informal sector workers and proprietors. But the working of private markets have not been able to fill this void; while there are numerous private markets initiatives, these have been insufficient both in quantity and skills coverage.

Training markets have failed to develop due to market imperfections on the side of both demand and supply. Effective demand (and a willingness to pay) for external training may be stunted for many reasons, including a lack of awareness of individual skill shortcomings and of information on economic opportunities for use of any newly acquired skills. And there is a two–way information problem, in that the lack of training supply means that potential trainees have little scope to develop knowledge about training opportunities, since these are potential only, and not available in the market. On the other hand, there is little incentive for new suppliers to emerge, given the lack of demonstrated demand and the risks involved in pioneering new training forms to meet the requirements of the sector.

This defines a central role for government (or training authority or donor) in developing these training markets. Most initiatives have been on the supply side, in the provision of courses leading to self–employment in newly developing markets (Tanzania and Madagascar). Others have been directed towards 'in–service' skills acquisition (Cote d'Ivoire, Kenya, Zimbabwe).

Some initiatives aim at generating effective demand for these training courses and increased cost–sharing. In the case of the voucher scheme in Kenya an additional effect has been the identification (and supply response) of a novel form of training provision for the sector in the form of courses put on by master craftsmen, within a familiar work–shop setting. But generally, because effective demand for these courses is weak, they remain very heavily subsidized.

How may this substantial subsidy be justified? The case is strongest (on social grounds) for pre–entry courses that facilitate transfer into self employment; these are frequently targeted at disadvantaged and poverty groups – rural women for example – and we have argued above that there is wide agreement on the legitimacy of a financing role for government here. Cost recovery can only be minimal in these cases. The case is less clear for in–service training, especially over the medium term. This training provides few of the wider, externality benefits that might justify subsidy and an ability (though not willingness) to pay is not clearly lacking. The case for subsidy is even less strong on benefit grounds for inter–firm cross–subsidization, financed through levy payments by formal sector enterprises. However, a number of countries have moved in this direction (Cote d'Ivoire, South Africa). These considerations highlight the need to employ training subsidies as an interim, learning tool, with increased cost–sharing gradually replacing the subsidy. But most schemes have been able to move only slowly in this direction. The emergence of independent, self–sustained training markets for the informal sector remains a long way off.

11 Financing Mechanisms: Contribution to Broad Policy Objectives

In this paper we have examined, in a SSA context, the use of various funding mechanisms for financing training. The focus of this chapter is rather different. Ultimately, government establishes a financing framework in order to achieve a range of prescribed policy objectives in the training sphere. Financing mechanisms can make a contribution to reaching these policy objectives; in constructing a financing framework for the training system, government will be cognizant of the role that particular financing mechanisms (which constitute part of the financing framework) can play in achieving this broader range of policy objectives..

In this chapter we identify fifteen major policy objectives that governments may pursue; against each objective we list those financing mechanisms that can play a role in moving towards achieving the objective. Some mechanisms will be relevant to more than one policy objective.

In Table 11.1, we outline this matching system between general policy objectives in the training sphere on the one hand and between those measures (discussed at various points in the paper) that may be employed in order to achieve them, on the other. Drawn from the discussion in earlier chapters, the strengths and weaknesses of these mechanisms are recorded and SSA country examples noted. The table might serve as a checklist for policy makers, and their advisors, for probing the menu of available finance interventions that may be employed, alone or in concert with others, to reach a desired policy objective.

Table 11.1
Policy Objectives and Financing Mechanisms, SSA

Policy Objective	Financing Mechanism	Financing Mechanisms: Notable Strengths(S) / Weaknesses (W)	SSA Country Examples
1. Raising additional or alternative funding for public sector training	Earmarked training taxes (usually based on company payroll)	Can provide a stable and protected source of funding for national training provision (S)	Tanzania
		Employers may shift the incidence of the levy on to workers in the form of lowered wages; then workers and not the employers bear the burden of the tax (W)	
		Payroll levies may constitute an over-sheltered source of funding, leading to unspent surpluses, inefficiencies and top-heavy bureaucracies (W)	
		Employers may shift the incidence of the levy on to workers in the form of lowered wages; then workers and not the employers bear the burden of the tax (W)	
		Payroll levies marginally raise the cost of labor to employers, possibly discouraging employment (W)	
		Earmarked taxation do not conform well with the principles of sound public finance and weaken attempts to unify the national tax system (W)	
		Under fiscal pressure, government may	

		incorporate training levy proceeds into general public tax revenues (W)	
		Levy proceeds may be diverted to non-training uses (W)	
	Co-financing (matching funds)	Exerts pressure on training institutions to generate funding (S)	
	Cost sharing (particularly, trainee fees)	Trainees legitimately share in the cost burden of human capital creation, from which they are direct beneficiaries (S)	Kenya (Jua Kali project)
		The poor may be excluded from training opportunities unless targeted subsidies/scholarships are available (W)	
		Under fiscal pressure, government may incorporate training levy proceeds into general public tax revenues (W)	
	Deferred trainee fees (government secured or subsidized loans)	Availability of trainee loans facilitate a policy of raising training fees and cost sharing (S)	
		For most SSA countries where student loans are in place, the track record has been poor; loans for trainees will not fare better (W)	
	Revenue generation by training providers:	Renting out facilities: fuller use of otherwise underutilized facilities (S)	Tanzania Botswana
	Production-for-profit/training-with-Production	May lead to training outcomes more closely geared to the needs of the market (S)	Botswana
		Neglect of the training function, lowering the quality and quantity of training (W)	
		Too many resources may go to production activities rather than training (W) Income may not remain with the training institution (W)	
	Promoting private training provision	Expansion of the national training system can be achieved without	

		commitments of public funds (S).	
		The concentration of private providers on low cost, high demand courses, may leave public sector institutions with the more costly, technical courses and limited possibilities for across-course	
		subsidization (W)	
	Donor aid (grants, loans)	Donor aid may be earmarked for training that is not appropriate for the country setting (W)	Madagascar
2. Promoting enterprise-based training (formal sector)	Fiscal incentives: company income tax concessions	Requires a well-developed and broadly-based system of corporate taxation (W)	Mauritius
		Cost burden of the scheme falls largely on public budgets – reduced revenues (W)	
		Responsiveness of firms often low because few firms earn sufficient profits to benefit from the tax exemptions (W)	
		Firms may not respond to the tax incentive or may benefit from the subsidy without increased training efforts (W)	
	Subsidies/grants from Government or National Training Fund	Cost burden falls on public budgets – increased public expenditures (W)	Madagascar
		Firms may not respond to the incentive or may benefit from the subsidy without increased training efforts (W)	
	Levy-grant systems: training cost reimbursement, training levy exemption, training cost redistribution	May facilitate a more systematic, structured approach to enterprise training (S)	Cote d'Ivoire Mauritius Nigeria
		Given their particular training needs, many firms, particularly small ones, do not benefit from the scheme; this breeds resentment, opposition and compromises the status of	

		training levies as "benefit taxation" (W)	
		Firms may not respond to the incentive or may benefit from the subsidy without increased training efforts (W)	
	Industry training boards	May offer training promotion, advisory and other services (S)	Kenya Nigeria
		May be ineffectual unless has genuine authority, autonomy and stakeholder representation (W)	
	Training quotas	May be too blunt a weapon to take account of differing training needs across firms and sectors (W)	? Not in SSA
		Firms may find it preferable to pay a fine for non-compliance rather than invest sufficiently in training provision to meet the quota (W)	
	Promoting "modern" apprenticeships		South Africa (learnerships)
	Legislation: training investment protection		
3. Improving efficiency and effectiveness of public training institutions	Output-based funding of training institutions	Introduces equitable and objective criteria for funding allocation (S)	
		Promotes demand-driven training (S)	
	Competitive bidding for funding, by training institutions	Competition lowers public cost of training support (S)	South Africa Cote d'Ivoire Senegal
		Bidding that is open to private as well as public training providers – strengthening the movement towards lower cost provision (S)	
	Decentralization/institutional autonomy	Local institutional initiative better able to identify and meet local training needs (S)	Madagascar Mauritius Tanzania –planned
		Local autonomy in budgetary allocations will facilitate development of locally –appropriate,	

		demand-driven training (S)	
		If carried too far, central coordination of the training system may be placed in jeopardy (W)	
		Local management of training institutions may be weak in the absence of appropriate staff development (W)	
	Contract training	Secures required skills development for special target groups (S)	
4. Effective allocation of national training resources	National training authorities	May be unsuccessful unless sufficiently well resourced, with access to required expertise (W)	
		May be ineffectual unless has autonomy, genuine authority and stakeholder representation (W)	
	Partnership: participation of stakeholders	Substantial representation of the major stakeholders on management board engenders a sense of ownership and cooperation in national resource management and facilitates (S)	
5. Moving towards flexible, market-responsive Training provision	Promoting private training provision	The concentration of private providers on low cost, high demand courses, may leave public sector institutions with the more costly, technical courses and limited possibilities for across-course subsidization (W)	
	Outcomes funding of training institutions	Strong financial incentives to eschew supply-dominated institutional training (S)	
	Contract training	Secures required skills development for special target groups (S)	South Africa
	Decentralization/institutional autonomy	Local institutional initiative better able to identify and meet local training needs (S)	Kenya
		Local autonomy in budgetary allocations will facilitate development of locally -appropriate,	

		demand-driven training (S)	
		If carried too far, central coordination of the training system may be placed in jeopardy (W)	
		Local management of training institutions may be weak in the absence of appropriate staff development (W)	
	Training vouchers/accounts	Promotes consumer/trainee choice (S)	Kenya
		Can develop effective demand (willingness to pay) for training (S)	
6. Equity objectives: training for minorities and special/disadvantaged groups	Normative financing for disadvantaged groups		
	Targeted scholarships		
	Targeted vouchers	Promotes consumer/trainee choice (S)	
		Can develop effective demand (willingness to pay) for training (S)	
	Special allocations from Training Funds, particularly when financed by payroll levies	Training levies collected from formal sector employers can serve as a vehicle for cross subsidization of training, from the formal sector to minority and special groups (S)	South Africa
		May be opposed by formal sector firms, as weakening the benefit principle of training taxes (W)	
7. Equity: training/retraining the unemployed	Contract training	Secures required skills development for special target groups (S)	
8. Equity: meeting the needs of disadvantaged regions	Regionally targeted special allocations from Training Funds	Regionally-based funding allocations may be self-serving if subject to political pressures from local vested interests (W)	Tanzania (not well implemented)
	<i>Regional</i> training boards	May be difficult to maintain a balance between central coordination and local autonomy (W)	Tanzania Madagascar

<p>9. Improving training for the informal sector and for self-employment</p>	<p>Training Funds</p>	<p>Training levies collected from formal sector employers can serve as a vehicle for cross subsidization of training, from the formal to the informal sector (S)</p>	<p>South Africa</p>
	<p>Vouchers</p>	<p>Promotes consumer/trainee choice (S)</p>	<p>Kenya</p>
		<p>Can develop effective demand (willingness to pay) for training (S)</p>	
<p>10. Attracting foreign physical investment</p>	<p>Subsidized training for foreign companies which establish new, local production facilities</p>		<p>? Not in SSA</p>

12 Lessons for Policy: Conclusions and Overview

This concluding chapter pulls together major lessons for policy. It is essentially practical in aim. It presents a range of conclusions, culled from the more detailed presentation in preceding chapters, which relate to the efficacy of current training finance practice in SSA countries. This discussion is set out within the unifying framework of what we have described, in the introductory chapter, as the "emerging consensus" relating to training finance in developing countries.

12.1 Major Policy Messages

In Chapter 1, we outlined an emerging consensus relating to the desired directions for reform for the funding of training in developing countries. The major elements of this policy consensus, summarized in Table 12.1 (reproduced from Table 1.1, below) have constituted the underlying themes of the present paper. It is within the framework of this policy consensus that we present the major policy messages emerging from this study.

There is now considerable agreement on what should constitute the main objective of training policy: this may be defined as "facilitating the development of effective, efficient, competitive, flexible and responsive (demand-driven) training systems, to meet national economic and social needs and the needs of individuals." Well-functioning training systems should reflect all five of these characteristics. We consider fifteen finance-related issues that impinge on the goal of reaching this overall policy objective.

12.1.1 Redefined Government Role

The dominant role played by government in both the financing and provision of training is excessive in many SSA countries. While there is probably much more public *provision* of training than is required by economic rationale alone, this may not be sub-optimal if public training is efficient, effective and market-responsive; unfortunately, frequently, this is not the case. And again it seems to be the case that there is far more public *financing* of training than is justified by the economic arguments adduced in Chapter 3, above. Constrained national budgets have exerted their toll on the quality and effectiveness of public training provision. These increasing pressures on government budgets provide an opening for the diversification of funding for training – a major theme of this paper.

The appropriate role of government in training markets cannot be determined without reference to the capabilities of private training markets. Where they can function well, they can be seen as an alternative to public sector provision; where they do not, then the public sector should be engaged. This approach to the appropriate role of government in training finance and provision requires a country to determine its individual needs for public sector training intervention. It will need to examine the performance of its markets, the capacity of the private sector to deliver training and its own preferences with regard to social policies and equity. On this basis, there is likely to remain a central and continuing role for the state in most countries in the delivery and, particularly, in the financing of training.

Table 12.1 (based on Table 1.1)
Training Finance: The Emerging Policy Consensus

Overall training policy objective:	
To facilitate the development of effective, efficient, competitive, flexible and responsive (demand-driven) training markets, to meet national economic and social needs and the needs of individuals	
Role of training finance in moving towards this objective	Explanation
1. Redefined government role	Redefinition of government role (diminished, but still critical), entailing reduced public budgetary support for formal sector institutional training
2. Funding diversification	Diminished government financing role is to be accompanied by a diversification of sources of financing, greater cost recovery and cost sharing
3. Cost sharing	Moves towards increased cost sharing, with higher, more realistic training fees (with scholarships for the needy) and perhaps state-backed student/trainee loans
4. Training levies	Funding diversification measures to include training levies on enterprises
5. Income generation	Funding diversification measures also include income generation by public training institutions
6. Decentralization	Income generation objectives would be furthered through decentralization of control over public sector providers and greater institutional autonomy
7. Private sector	Government to encourage private sector provision of training
8. Funding public training institutions	Replace arbitrary, <i>ad hoc</i> funding arrangements by objective formula funding related to inputs, outputs and outcomes. Consider case for subsidy of selected private training institutions
9. Trainee/consumer choice	More voice is to be accorded to trainee/consumer choice; vouchers may help develop the demand side of the market where subsidy needs to be retained
10. Levy –grant	Levy–grant mechanisms to be introduced where formal sector enterprises under-train
11. Training funds	National training funds to be developed, to take a broader and longer term view of training expenditures in a national context
12. Training authorities	Where institutionally possible, fully–fledged, autonomous national training authorities to be established
13. Stakeholders	Increased participation of stakeholders (especially employers) in national training policy formation and execution
14. Disadvantaged groups	Continuing and enhanced government role in skills development as an integral part of a package of measures to assist disadvantaged groups
14. Informal sector	Central attention to be paid to largely neglected training needs of small micro enterprises and informal sector producers

12.1.2 Funding Diversification

In national training systems where public training budgets are constrained, it is usual to develop for augmenting resources available for training programs entailing a combination of such measures as reduced training subsidization and the increased sharing of the training finance burden by other beneficiaries of the training system, particularly trainees and enterprises – a process refereed to as funding diversification. Funding diversification can take many different forms. Chapter 7 outlines four different avenues that may be pursued; separately or in combination. Three act directly in bringing in additional revenues to the training

sector while the fourth affects training budgets only indirectly. Thus, additions to total funding available for allocation to training providers may be secured through the levying of payroll taxes. Again, training institutions may augment public budgetary allocations through cost sharing (in particular through introducing or raising course fees) and through income generation (largely from combining production with training). And, finally, encouragement may be given to the development of private training institutions.

These diversification options are not alternatives; all four avenues may be explored simultaneously. However, whether or not to do so and to what extent, remains a policy issue that must be settled within the context of conditions ruling in each country situation.

12.1.3 Training Fees

Moves are common in many countries towards increased cost sharing, with the imposition of higher, more realistic training fees, scholarships for the needy and perhaps state-backed student/trainee loans. There is little conformity of practice in tuition fees policy across countries. The feasibility for tuition fee setting (in relation to unit costs of training) is a compound of many and diverse factors; these will vary from place to place. They include: type and costs of training, the price elasticity of trainee demand for different training courses, political constraints and policies for equality of opportunity. Thus it is not possible to be prescriptive in relation to the scope for generating revenues from tuition fees; this will need to be settled on a case-by-case basis, in the light of local conditions and possibilities.

A central issue in fee policy is whether a regime of standard, national-wide compulsory fees should be instituted or whether freedom should be accorded to individual training institutions to fix the level of fees overall, and differing by type of training course. Institutional autonomy in the setting of fees, while representing a more desirable approach, may not be feasible in otherwise centralized training systems. But while standard, compulsory fee setting may be an inflexible tool, unlikely to reflect local market realities it is generally acceptable as a second-best measure.

The positive financial benefits from greater cost recovery need to be examined alongside the potentially adverse effects on equity. There is a clear trade-off here. Higher, realistic fees will exclude from training those who are unable to pay; fees set at comfortably low levels will fail to make a sizeable contribution to cost recovery. In particular, negative impacts on the access to training opportunities of the poor, minorities, rural populations and other disadvantaged groups are likely to ensue. This points to the widely recognized need to introduce targeted subsidies directed to these at-risk groups, in the form of scholarships and reduced fees. However, targeting those *most* in need within these groups, particularly in the SSA context, has proved to be no easy matter.

Cost sharing through the use of user fees will discourage participation in formal training programs, even by the non-poor. The classic solution to this problem, encountered most frequently in higher education, is deferred cost recovery in the form of student loans schemes. But the track record for student loans schemes in SSA countries, is poor. The sound administration of a loans scheme requires appropriate, high level, institutional support – at a premium in many SSA countries. Given the lack of success in administering student loans scheme in SSA, it is improbable that training loans would fare better.

12.1.4 Training Levies

In many countries, particularly in Latin America, the dominant tool for funding augmentation is the training levy, usually levied as a percentage of payroll. Levy proceeds are used mainly to support public sector training provision, with the emphasis on initial training at formal public training institutions.

In the SSA context especially, payroll levy schemes of this type (though not very widely adopted) may be seen as a valuable mechanism for greater funding diversification, lightening the burden of training funding falling on the state. The expectation is that levy income would constitute a complement to existing government financing, thus providing an additional source of funding; this has not always been the case in practice. In addition to generating more funding for training, levies of this type can offer a more stable form of funding than is forthcoming from government allocations. However, the success record of training levies in SSA countries appears to be less than in other regions; while working well in some SSA countries, training levies have been found to be wanting in others. Thus, particular attention will need to be accorded to levy scheme design in order to avoid some of the weaknesses that have been evident in the SSA context. These include poor levy collection outcomes, leakage of levy proceeds into general government revenues and inequitable coverage (in terms of firm size and sectors to be included).

The scope for levying payroll taxes is well established by international experience in SSA countries and elsewhere: almost all countries that have introduced payroll levies have set the levy rate in the range of one to two percent of company payroll bills, the majority at the lower end of the range.

12.1.5 Institutional Income Generation

Income generated from the sale of production and service activities of trainees can constitute a useful form of additional institutional income. Income may be derived as a byproduct of the training process itself. But it is possible, more purposefully, to utilize available skills and facilities to produce output for sale in the local market; indeed, exposure to local markets may lead to more relevant, market oriented training. Here the issue is one of maintaining a healthy balance between these two activities. As more weight is given to instruction, the income potential from production declines; alternatively, quality of training will suffer as emphasis is placed on production rather than instruction.

The proportion of recurrent expenses that can be covered by production sales will vary considerably from case to case; the scope for income generating from production will depend on numerous local factors, including the nature of the product, local demand conditions and potential market competition. If an acceptable balance is maintained between training quality and production for sale, the scope for cost recovery may be fairly limited, usually accounting for only a few percent of recurrent expenditure. In some exceptional cases, however, it can contribute a considerable proportion of total costs.

Training institutions may also generate income from the sale of services, including the renting out of underused facilities and providing consulting services to local enterprises.

As with training fee policy, local institutional initiative in income generation from production will be stunted if this income does not contribute to institutional budgets; this is the case where the sums collected are deducted from institutional budgetary allocations and thus accrue to government budgets or the national training fund, and not to the training institution.

12.1.6 Decentralization

Institutional fee charging and income generation objectives can be furthered through decentralization of control over public sector providers and greater institutional autonomy. Where the imposition of user fees are voluntary and left to local institutional initiative, they may encourage training providers to develop a more dynamic, even aggressive, approach to exploiting the potential of the local market environment. In this way institutional fee policy becomes more than a device for cost recovery and cost sharing: In providing a mechanism for varying fee levels across courses and client groups it serves as a tool for moving the training system towards an environment characterized by open, demand-oriented training. In many cases, this condition is unmet. More generally, it is recognized that fee policy and income generation is not set in a vacuum. Institutional-level fee fixing is usually but one element (ideally a central one) of more general, decentralized training systems with local institutional autonomy. It is only in this more liberal context that the full potential of cost sharing and income generation is likely to be forthcoming.

12.1.7 Private Sector Development

The growth of private training institutions, with trainees paying full costs provides represents a pathway for expanding the national training system without heavy commitments of public funds. Indeed, *reduced* public training provision could be possible (and concomitant budgetary reductions) with the reduction in public training supply made up by compensating expansion of private training institutions.

In many countries, the lack of private training provision results from financial, institutional and other constraints, holding back private provider development. The imposition of restrictions such as legal prohibitions, tight regulatory control and tuition fee ceilings may combine to render private institutional start-up very problematic. While these restrictions are intended to protect the interests of potential trainees, they are often counter-productive in constraining private training supply. Governments can help establish a more liberal regulation regime, particularly aimed at quality control, combined with an enabling environment encouraging the flowering of incipient private training institutions and the improved dissemination of information about quality of training institutions and courses and their relevance to employment opportunities.

12.1.8 Funding Public Training Institutions

An important task of funding disbursement policies, as discussed in Chapter 8, is to provide an appropriate mix of regulation and incentives to ensure public training can hold its own in an environment of competitive training markets. A much needed reform are moves towards the gradual dismantling of the arbitrary, *ad hoc* institutional core funding arrangements in place in almost all SSA countries, and their gradual replacement by objective funding formula, such as those related to inputs, outputs and outcomes.

12.1.9 Trainee/Consumer Choice

In the process of moving away from supply-dominated training markets, more emphasis needs to be accorded to developing trainee/consumer choice. Both increasing cost recovery at public training institutions through higher tuition fees and the development of private training provision will facilitate the development of the demand side of training markets, in which the consumer (trainee) will have a more central role. However, trainee choice needs to be an informed choice. But relevant information on training opportunities and the relative advantages of various course offerings and institutions is often lacking, as is information on the relevance of courses to labor market demands; there is a clear role for government intervention here in providing potential trainees with such information.

Where training subsidy needs to be retained, vouchers of entitlement to training courses may help to develop further the demand side of the market; however, while training vouchers are rare in SSA countries, some training systems have initiated (limited and largely experimental) voucher schemes whose progress will be monitored with interest.

12.1.10 Levy-grant Systems

Where formal sector enterprises under-train, there may be a strong case for encouraging enterprise training through training incentives and a particular case can be made for subsidized apprenticeship wages on both equity and efficiency grounds. Levy-grant systems (where the training grant to the enterprise is financed by a training levy) have some clear advantages over alternative incentive systems, notably direct government subsidy payments and concessions on enterprise tax obligations of indirect for companies that train. However, all three mechanisms share a number of weaknesses. As discussed in Chapter 9, these include the receipt of unnecessary windfalls, the encouragement of training distortions, repackaging, high inspection costs and heavy administrative burden on the firm. A central problem in training grant design is to minimize the effects of these weaknesses.

A major advantage of levy-grant systems is that they do not draw on public funds, a point of some importance in times of parsimonious government budgets; in addition, they can lead to more systematic, structured enterprise training (though often are not designed to do so). On the other hand they may result in between-firm inequities if there is no close relationship between the burden of the levy and the benefits received.

The disadvantages of tax concession schemes have militated against their adoption in other than a very few countries.

2.1.11 Training Funds

A national training fund may be seen as a unique institutional framework for unifying and augmenting public sources of funding for training and for allocating funds in line with national policies and priorities. While in older established training funds, training levies were the dominant (usually only) income source, newer funds draw from a variety of available income sources, including government budgetary allocations, donor funding and income generated by the fund itself. Indeed, in some cases training funds derives no income from training levies; either levies have not been instituted or, where in place, levy proceeds are regarded, in practice, as general tax revenues and not passed on to the fund.

With the broadening of income sources of training funds, training funds are now increasingly regarded as a general funding pool, distributed across various recipient destinations according to established priorities and policies; this results frequently in a considerable degree of cross-subsidization of training (especially of informal sector training from formal sector levy proceeds). Successful fund management seems to require autonomy of the management board in decision-making and its control over budget allocations; also substantial representation of the major stakeholders on management board (especially employers), engendering a sense of ownership, appears to be an additional ingredient of success.

An important objective of establishing national training funds (particularly when financed by company training levies) is to provide sustained and stable funding for the training programs they support. In practice this has not always been achieved, notably when funds do not receive the resources that have been designated to finance its activities; training levy proceeds, designated for the training fund, may be absorbed instead into general government revenues. Training fund sustainability over the longer term constitutes a serious problem in some countries, in particular where training funds have been launched by donors and are funded, in the main, externally. This problem of fund sustainability will be endemic in those many SSA country situations where public budgets are likely to be severely constrained over the medium term and where the time is not ripe for the introduction of training levies. In this situation, over-generous external support for national training funds, without the planned, complementary development of domestic funding, will result ultimately in moribund training authorities and empty coffers.

12.1.12 Training Authorities

Where institutionally possible, fully-fledged, autonomous national training authorities to be established, charged with the central role of assuming responsibility for national skills development. To respond to the developing skill needs of the economy and to be in a position to be proactive, rather than just responsive, in relation to ongoing technological and industrial change, public training systems need a greater degree of independence than is forthcoming from line ministries. National training authorities will often play a central coordinating role in planning the national training system, in developing training policy, supervising national skills testing and certification as well as providing necessary information services and developing appropriate labor market signals.

12.1.13 Stakeholder Role

Participation of the main stakeholders (especially employers) in national training policy formation and management (such as through active membership of the governance institutions of training funds or national training authorities) has an important role to play in building consensus on training issues; this may be particularly important where enterprise training levies are in place.

12.1.14 Needs of Disadvantaged Groups

A continuing and enhanced government role in skills development should form an integral part of a package of measures to assist disadvantaged groups. There is an increasing social awareness (and conscience) concerning the low current status and skill needs of special groups, such as the poor, ethnic minorities and women. In parallel, there is wide acceptance of the view that the government has an obligation to assist in this field, through financing and perhaps provision of special programs, aimed particularly at securing entry into the informal sector. These developments are likely to be heavily constrained by lack of available government funding because they are coincident with increasingly limited public budgets and greater inter-sectoral competition for funding allocations. This may indicate an appropriate role for donor intervention.

12.1.15 Informal Sector Training

Central attention needs to be paid to the largely neglected training needs of small micro enterprises and informal sector producers. Throughout SSA countries, considerable population (and labor force) growth, combined with minimal employment increases in the combined public and formal private sectors, place an increasing absorption burden on the informal sector. While traditional informal sector training markets, characterized by non-structured within-firm skills acquisition, continue to serve the sector well, the system is proving too narrow to cope with the increasing challenges emanating from technical change, skills enhancement and the widening of geographical markets. Public institutional training has not been able adapt to the particular skill needs of the informal sector. Thus an increasingly central role for specialized training providers (external to the firm) is now seen, both for entry training into new skill areas and developing markets as well as for informal sector workers and proprietors; private markets have not been able to fill this void, thus defining a critical role for government initiatives, perhaps buttressed by donor support.

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Endnotes

¹ A revised version appears as Chapter 4, in Middleton Ziderman and Adams (1993).

² A shorter, revised version is available in Dougherty and Tan (1997)

³ See Lauglo (1992) and Bennell (1996)

⁴ See also the discussion in Middleton, Ziderman and Adams (1993); a technical presentation is provided in Katz and Ziderman (1999)

⁵ Drake (1991) also discusses financing modes in an evolutionary context. Focussing on training finance regimes in industrialized West European economies, he identifies four forms of market intervention along a continuum ranging from 'pure bureaucracy to pure market'. These are defined as market-displacing,

market-supplementing, market-regulatory and market-reliant modes. While our two approaches have commonalities, Drake's relates to training regimes in industrialized economies while the focus here is on training finance in developing countries.

⁶ A somewhat dated, though still highly relevant discussion of national training agencies (and funds) is given in Herschbach (1990)

⁷ The following discussion is adopted from Johanson (2001a)