Public Financing of Vocational Training through Competitive Funds:

A Promising Option for Latin America and the Caribbean

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Labor Markets Division

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PUBLIC FINANCING OF VOCATIONAL TRAINING THROUGH COMPETITIVE FUNDS: A PROMISING OPTION FOR LATIN AMERICA AND THE CARIBBEAN

TECHNICAL NOTE

LABOR MARKETS DIVISION

SOCIAL SECTOR

INTER-AMERICAN DEVELOPMENT BANK

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May 2017

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The objective of this Technical Note is to describe the way competitive funds operate, based on examples from developed countries. The ultimate goal is to inform and guide its possible design and implementation in Latin American and Caribbean countries. The selected examples offer interesting contrasts due to the heterogeneity of their design, objectives and operation. In addition, these are new funds that were recently designed by the respective governments, with the purpose of introducing improvements in public policies for financing job training. The document is divided into two sections. In the first section, a conceptual framework is presented which seeks to understand the benefits of competitive funds to finance training. In the second section, specific examples are described: three projects in developed countries (New Zealand, United Kingdom and Michigan State in the United States) and one in a small developing economy, Barbados. Finally, the last section presents conclusions and identifies the challenges to be considered.

JEL codes: J24, J0, H41.

Keywords: Training, competitive fund, human capital, skills, productivity, public finances.

CONTENTS

Acronyms

BIS	Department for Business, Innovation and Skills
BVTB	Barbados Vocational Training Board
CBTF	Competency-based Training Fund
CVQ	Caribbean Vocational Qualifications
DFS	Direct Finance Scheme
EOP	Employment Ownership of Skills Pilot Round
ETF	Employment and Training Fund
IDB	Inter-American Development Bank
INADEH	National Institute for Vocational Education and Training for Human Development
INEFOP	National Institute for Employment and Vocational Training for the Private Sector
IT	Information Technology
ITF	Industrial Training Fund
ITO	Industrial Training Organizations
LAC	Latin America and the Caribbean
MGF	Matching Grant Facility
MWA	Michigan Works! Association
NVQ	National Vocational Qualifications
NZQA	New Zealand Qualifications Authority
OECD	Organisation for Economic Co-operation and Development
SENA	National Learning Service
SFA	Skills Funding Agency
SGS	Skills for Global Services
STM	Standard Training Measure
STTF	Skilled Trades Training Fund
TEC	Tertiary Education Commission
TEO	Tertiary education organizations
TVET	Technical vocational education and training
UKCES	UK Commission for Employment and Skills
WDA	Workforce Development Agency
WIA	Workforce Investment Act
WIB	Workforce investment boards

1. Introduction

In the past decade, the economy of Latin America and the Caribbean (LAC) buoyed largely by a positive external context, enabling it to produce significant social gains, among them the reduction of inequality and poverty. However, the future is not looking as rosy, and the only way to safeguard the progress made is to buttress internal and structural growth determinants, one of which is workforce productivity, where immense challenges still remain.

Workforce productivity in the region has virtually stagnated in the past two decades and has lost ground in comparison with that of other emerging economies. This poor performance in productivity is largely the result of skills deficits in the workforce. Businesses in LAC have a harder time meeting their skills demand than those in other emerging regions. Formal businesses in LAC are three times more likely than their counterparts in South Asia to see their operations hindered by a lack of skills in the workforce (OECD, 2015).

Tackling this challenge requires tailoring the supply of skills to the demand of the productive sector, focusing more intensely on business needs. There has traditionally been a disconnect in LAC between the vocational training market and the job market. Public funds have customarily been channeled to national educational institutions and training programs in which employers have rather limited input (González-Velosa et al. 2012), reflecting an institutional structure that does not promote a flexible supply of skills nor meet the real challenges of gathering information on skills needs and translating that information into relevant curricula in training programs.

The developed world is not exempt from these problems. In some industrialized countries, the government has therefore begun introducing innovative public financing schemes to incentivize employer leadership and facilitate more flexible and demand-driven training. The result has been growing use of **competitive funds** awarded directly and competitively to the productive sector to finance skills development.

Competitive funds are designed to ensure transparent and participatory resource allocation that directly addresses the needs of the productive sector. Typically, these funds are competitively awarded to businesses and/or business consortia and training providers on the basis of transparent selection criteria. The selection process usually considers aspects such as cost-effectiveness, relevance to the sector, and alignment with development priorities. Selection criteria can create incentives for businesses to ensure quality and coverage and promote public-private cofinancing arrangements. They can also encourage coalitions and ties between business and training providers for the execution of funds.

The purpose of this Technical Note is to describe how these funds operate through examples in the developed countries, with the goal of providing information and guidance for their potential creation and use in LAC countries. As a whole, the cases selected offer interesting contrasts due to the differences in their design, objectives, and mode of operation. Furthermore, they are new funds, recently designed by the respective governments to improve vocational education financing policies.

This Note is divided into two sections. The first presents a conceptual framework for understanding the usefulness of a competitive fund scheme in financing vocational education, the logic behind its design and implementation, and its advantages in terms of efficiency, transparency, and quality. It also introduces an alternative funding scheme – matching grants – and contrasts it with that of competitive funds, differentiating the situations in which each is more suitable.

The second section describes specific examples: three projects in developed countries (New Zealand, the United Kingdom, and the State of Michigan in the United States) and one in a small developing economy, Barbados. Each of the examples starts out with a description of the institutional environment and the role of the organizations involved, followed by the public financing system for training and the objectives and operations of the competitive funds. Although these funds have very different institutional and management schemes and different operating rules, the examples in this Technical Note have common features, objectives, and challenges that are summarized in the conclusions section. Finally, the last section provides some conclusions and identifies challenges to bear in mind.

2. What are competitive funds and what is their purpose?

The rationale for public financing of training through donations or grants is the presence of market failures and coordination costs that inhibit private investment. Many factors can lead businesses and workers to invest less in training than desirable for society as a whole. Businesses may invest less in training than desirable for the economy because of uncertainty about future returns. Strict regulations that limit wage adjustments may render investments in training unprofitable. Another factor is that businesses run the risk of investing in worker training and not reap the benefits of their investment if the workers quit and go to a competitor.

On the workers' end, there are also disincentives to investing in training. Like businesses, they have no way of accurately measuring the future returns on their investment. Moreover, it often happens that despite an interest in investing in skills development, workers have difficulty financing it when no credit instruments are available to them. In many countries, educational financing is geared more to academic programs than vocational training. Moreover, mechanisms to certify the skills and experience acquired through training are often lacking, making it impossible for the labor market to recognize and validate the learning.

The absence of formal mechanisms for dialogue between employers and training providers, and hence, the limited participation of the productive sector in identifying the demand for training profiles, is another critical issue in the training market, especially in emerging economies. The vocational training supply is often missing a productive perspective aligned with the needs of employers, leading to a vicious circle in which the training does not meet the needs of employers, who, in turn, have few incentives to participate in the process. This lack of coordination, added to the problems just mentioned, translates into insufficient investment and lack of relevance in vocational training. The effect is a disconnect between the supply and demand for skills, which ultimately hinders the productivity growth and the employability of human capital as an engine of growth.

These market failures provide the rationale for government financing of vocational education. Through a public tender and grant scheme, governments can boost the level of investment in training while fostering quality. In LAC, the main interventions take place through: (i) a public supply of training through public training institutions (for example, SENA in Colombia, System S in Brazil, INEFOP in Uruguay, INADEH in Panama, and HEART/Trust NTA in Jamaica); (ii) the funding of public vocational education programs (such as *Juventud y Empleo* [Youth and Employment] in the Dominican Republic, *Bécate* (Get a scholarship) in Mexico, *Jóvenes Productivos en Perú* [Productive Youth in Peru]); and (iii) fiscal incentives for in-house vocational training in businesses (such as *Franquicia Tributaria* [Tax Exemption] in Chile).

A much less common alternative in the region are competitive funds, whereby resources are competitively awarded to training initiatives designed by businesses or employer partnerships. Awards are based on previously stipulated public selection criteria. The process begins with a request for proposals. Once received, the proposals are evaluated by a committee of relevant stakeholders who select the ones to receive financing. The request for proposals can be broad, to finance projects largely determined by the participants. It can also be restricted to predetermined sectors or even specific projects.

Competitive funds are, first, a way to increase transparency and effectiveness in the use of public resources. By receiving the funds directly, businesses encounter fewer obstacles to measuring the relationship between investment and quality. Employers directly observe accountability and the benefits of training, while results-based awards create incentives for efficient resource use.

Second, competitive funds are also a way to promote leadership among employers and motivate them to take ownership of the training process, which is essential for guaranteeing its relevance. Since employers must draft their own proposals to obtain these funds, they are delegated the responsibility of identifying the skills needed for the job. This leads to training interventions that are more aligned with the real needs of productive sectors, heightening their strategic importance and the potential for boosting workforce productivity. Furthermore, if employers directly guide the process, the government can play a more strategic role in aligning training with economic and development objectives. For example, it can award funds to priority sectors or to the development of skills needed for changing technologies or emerging sectors, while at the same time focusing on regulatory aspects and monitoring results.

In many cases, the funds require employers to partner with training providers or educational institutions in the design of vocational education programs, leading to the emergence of entities for continuous participation and dialogue between the training and productive sectors. This fosters competition among training providers and encourages higher quality training, giving providers an opportunity to improve their programs and develop more innovative solutions through closer ties with the productive sector. Competitive funds can also foster institutional change and improvements in public sector management, since insofar as they encourage collaboration, transparency, and more efficient use of resources, they will become a platform for strengthening institutions in the vocational training market.

Third, since these funds delegate the decision about the type of training, qualifications, and providers needed to employers, they create greater incentives for private investment in training. In some cases, they explicitly promote public-private cofinancing through incentives. In any case, since financing through donations or grants is a policy instrument, it must be coordinated with other public interventions.

To continue, the design and implementation of competitive fund schemes pose certain challenges. On the one hand, as funds for short-term financing, their sustainability may be at risk if the beneficiary institution does not achieve the sound financial footing required to continue the project without those resources. On the other, there must be a broad and diverse universe of potential applicants to the fund, because otherwise, proposals lacking the necessary quality and relevance could be financed. It is also important to prevent selection bias toward proposals from large enterprises, since the function of competitive funds is to finance proposals that could not be implemented in their absence. It is therefore essential to ensure that institutional and public administration capacities exist, which will guarantee the good use public funds to meet the desired objective.

An alternative financing scheme is **matching grants**, whose main characteristic is that they are awarded on the basis of the counterpart funds provided by the beneficiary. Matching grants are primarily used to support private-sector proposals, and unlike competitive funds, they are not competitively awarded as a rule. Any proposal that meets the stipulated requirements can be funded.

The main characteristic of matching grants is that, as subsidies leveraged with contributions from the beneficiary, they become an incentive for the private sector to invest and play a more active role. Projects financed with matching grants are generally less technical and geared more to fostering private-sector investment in new technologies, innovation processes, and other activities aimed at boosting the efficiency of production processes. The ultimate goal is to increase business profitability and support the creation of new businesses.

Thus, due to their competitive nature, competitive funds demand higher standards for proposals and higher levels of quality than do matching grants. Moreover, they are more useful for ensuring the transparency of information and promoting linkage among stakeholders. Matching grants, in contrast, facilitate project continuity and encourage greater private investment. By requiring contributions from the beneficiary, they facilitate the sustainability of projects over time. Given these differences, there are some schemes in which competitive funds and matching grants complement each other in a model that requires contributions from the beneficiary while competitively awarding the funds.

Competitive funds and matching grants are often used to promote innovative demand-driven initiatives in other sectors. In agriculture, for example, the use of competitive funds as a public financing instrument is becoming increasingly common (Box 2.1). In research and development, they are a well-established financing model. The majority of the OECD countries have competitive fund schemes of this type[2].

To summarize, competitive funds can be used to promote demand-driven investments in training, increase the relevance and quality of such investments, and promote productive linkages between business and training providers. In some cases, they can be

[2] For further details on the use of competitive funds for research and development, see: www.innovationpolicyplatform.org

supplemented with matching grants as an incentive for private investment. When deciding whether a competitive fund scheme is the right choice, it is useful to consider the objectives and do a cost-benefit analysis. This series of questions, adapted from the World Bank (2010) and van der Meer and Noordman (2004), can be useful for this analysis:

Analysis of market failures

a) Is there a failure in the training market? In terms of exactly which goods and services?
b) Would a competitive fund be an effective instrument for remedying the market failure? Would it eliminate the disincentives to investment in training?

Cost-benefit analysis

a) Would the benefits of a competitive fund outweigh the costs? The costs of implementing this type of model tend to be high and the benefits uncertain. What advantages does the competitive fund dynamic offer for remedying market failures? Is there a risk of undesirable side effects? If large projects are involved, they can lead to market distortions.

Analysis of implementation design

a) What are the eligibility criteria? Should the fund target a particular population? Access criteria are essential. It is important to confirm that the fund has no undesirable access barriers.
b) Is there institutional capacity to implement a competitive fund? Government and private-sector capacity to implement and administer competitive funds may be limited. Are there expectations of implementing future competitive funds that would justify investments in capacity building?
c) Are there mechanisms to ensure transparency and accountability throughout the process – or must they be created?

Box 2.1. Competitive funds for projects for innovative projects in the agricultural sector

The creation of competitive funds has become an increasingly common practice in the agricultural sector to spur innovation. These funds are used to finance projects for research and the dissemination and use of new technologies, and to better connect producers with the market and scientific institutions. In addition to encouraging innovation, the object is to open up greater opportunities for collaboration among innovative agents, agricultural producers, private investors, and public institutions, and to improve the institutional structure, since the proposals are drafted through partnerships among different stakeholders in the sector. Competition for funds promotes new lines of research and priority fields in science, increases the relevance and quality of scientific research, and encourages academic partnerships and more efficient use of resources, ultimately generating a more relevant and innovative scenario for knowledge production. Winning proposals are chosen by a panel of scientists after a rigorous review based on pre-set criteria. In almost every case, the fund requires counterpart contributions from the beneficiaries.

One of the advantages of a competitive fund scheme is its flexibility to target resources to strategic areas at the forefront of research that would not otherwise be prioritized and financed. At the same time, rigorous review and examination of the proposals can potentially increase their quality and relevance and build capacity among the beneficiaries. Collaboration among the different stakeholders in drafting the proposal can generate economies of scale for the use of resources, potentially boosting the efficiency of the investment. Finally, competitive funds for innovation have the potential to create innovative processes that can take root and become systematized on a wider scale, resulting in a sectoral or national innovation system.

3. Model experiences throughout the world

3.1 NEW ZEALAND

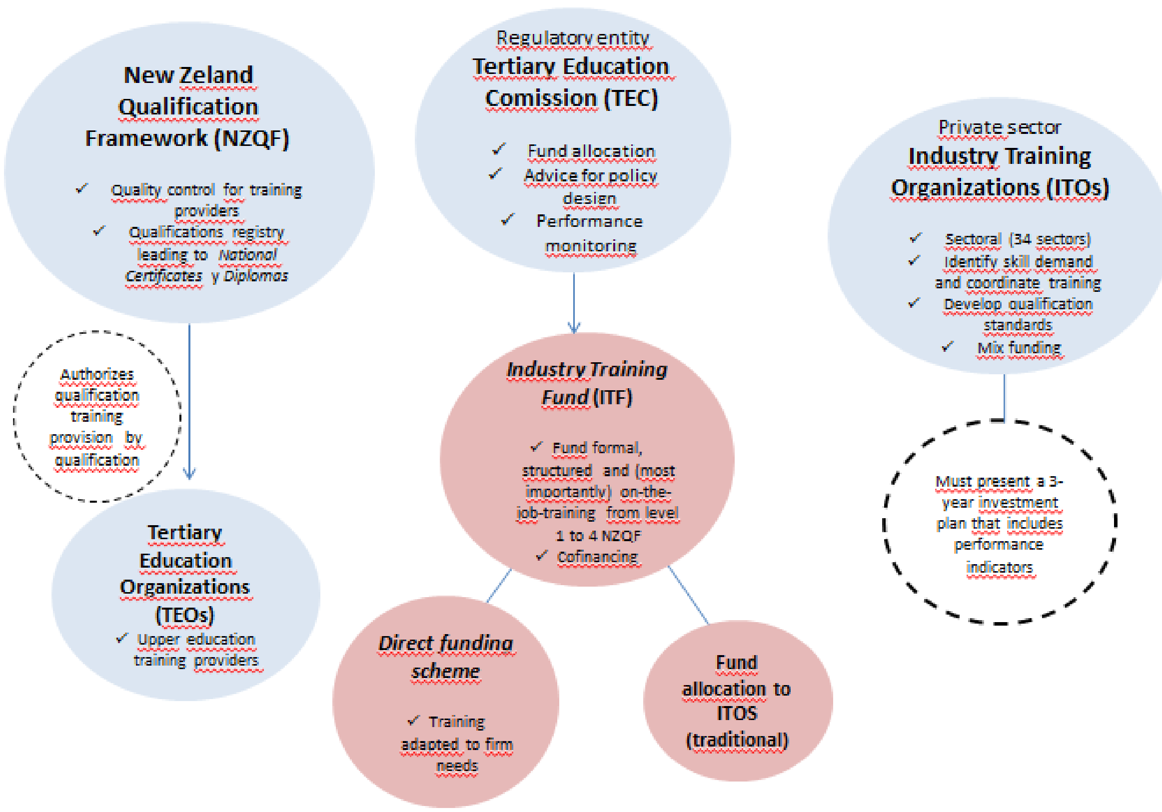
a. *Sector institutions*

New Zealand has developed a lifelong learning system that puts formal post-secondary education, on-the-job training, and vocational education under a single institutional framework. This framework, observed in countries that are successful in developing human capital, integrates educational systems with the labor market and promotes lifelong learning (Bassi et al., 2013; Crespi et al., 2014). Known as tertiary education, this framework is governed by the *Tertiary Education Commission* (TEC). Since 2003, the TEC has been responsible for planning sectoral policies and allocating public funds to the sector (approximately US$3 billion annually). This commission oversees policies ranging from university education to vocational education, apprenticeship training, and remedial reading courses for adults. Specifically, the TEC has three tasks: (i) allocate resources to tertiary education providers; (ii) monitor their performance; and (iii) provide information and advise the government in policy design.

Tertiary education providers are known in New Zealand as *Tertiary Education Organizations* (TEO). There are different types of TEOs. On the one hand are universities, which offer advanced academic and scientific research programs, and on the other, are vocational education providers of different types, including polytechnic institutes, private training establishments, and the *wananga* –providers who employ Maori educational techniques.

The productive sector coordinates training activities (in-house and elsewhere) through *Industry Training Organizations* (ITO), independent sector entities with two basic objectives: to develop plans and coordinate training matters (sometimes in the classroom but mainly in the workplace) and to develop educational standards (for example, qualifications development). ITOs are run by entrepreneurs, are recognized by the government, and receive both private and public financing. There are ITOs for different sectors and types of industries (plumbing, construction, agriculture, and even government and community services), for a total of 34. ITOs do provide training directly; their job is to identify skills demand in the sector and coordinate the teaching of those skills, serving as an intermediary between the productive sector and training providers. In this process, they design standards for qualifications that are then recognized by the New *Zealand Qualifications Framework* (NZQF), administered by the *New Zealand Qualifications Authority* (NZQA). In addition to registering training providers, the NZQA exercises quality control, authorizing them to provide training in the qualification area. Qualifications lead to different levels of national certification or diplomas and may be academic or technical (Figure 3.1).

Figure 3.1. Financing of training in New Zealand



Source: Prepared by authors

b. Public financing of training

With a tradition dating back to the 1990s (Diamond, 2003), New Zealand, together with Australia, has been a pioneer in the field of results-based public budget systems. Sectoral public expenditure in New Zealand is generally allocated through procurement contracts for products or results, in contrast to LAC, where it is traditionally based on inputs. The reason for shifting the focus from inputs to results and for allocating expenditure on the basis of performance indicators–with the consequent regulation and monitoring–is to create and leverage incentives for efficiency and effectiveness in resource utilization. Thus, New Zealand has a long tradition of performance-based contracts, the design of management indicators, and the creation of product costing systems. This was the context for the development of the tertiary education financing system.

Since 1990, this system has undergone four substantial reforms. The changes have always leaned toward a scheme that creates incentives for efficiency in resource utilization and quality in service delivery and at the same time is relatively simple to administer. Only 7% of employees receive government-subsidized training.

The TEC offers different types of public funds to finance training initiatives for workers, who can take advantage of different types of TEOs or ITOs. The most important of these is the *Industry Training Fund* (ITF), whose basic objective is to support productive-sector training initiatives. Specifically, the ITF is designed to help the productive sector finance formal structured training, chiefly in-house, at NZQF levels 1-4. These levels correspond to *industry training certificates*, issued to individuals with basic knowledge and skills for the workplace, continuing education, and/or work with the community. These certificates are the lowest level in the qualifications system, while levels 5 and 6 correspond to secondary school diplomas and 7, to a university degree.

The ITF is based on the principle of cofinancing. Thus, a prerequisite for securing these resources is that the cost of training be partially financed either by the employer or the worker who receives the training. Traditionally, ITF resources are allocated directly to ITOs. However, in 2014, a new pilot scheme was launched in which employers or employers' associations wishing to finance training offered by the TEOs, both in-house and elsewhere, can apply directly for ITF resources. This second model is known as a direct funding scheme, and since it is still in the pilot phase, its coverage is limited. ITF resource allocation is governed by different rules, depending on whether it operates under the traditional scheme or the direct funding scheme, as we will see further on.

Traditional ITF Scheme

In this scheme, ITF funds are allocated to the ITOs, which must use the resources to finance the development of training initiatives, but not provide the actual training; for that, TEOs must be contracted.

In order to compete for ITF funds, ITOs must submit a three-year investment plan to the TEC. This plan should have clear objectives and show that its proposals are aligned with the country's human capital development strategies (see Box 3.1, for example). Specifically, it should:

- Indicate how the plan meets the priorities of the government's tertiary education strategy and the demand for training identified in the sector.
- Determine what activities will be financed by the plan. Training activities and the development of new qualifications can be financed.

- Calculate the standard training measures (STM) that will be financed with the training plan, depending on the number of individuals registered in it. STMs are training measurement units equivalent to 120 educational credits that are used by the TEC as the basis for allocating resources[3].
- Specify the performance indicators and compliance targets, such as the number of people trained, the number of people who pass competency certification tests, and the number of new certifications developed.

Plans approved by the TEC receive funding based on the STMs. Since the fund operates on the principle of cost sharing, the government foots approximately 70% of the total cost of the training, with the remainder footed by industry and/or the workers. Industry also contributes in kind (logistics, for example).

Monitoring activities are a key part of ITF administrative functions. The TEC is responsible for supervising execution and the achievement of performance indicators and for conducting financial audits. TEOs, which are contracted to provide the training financed with the fund, are required to provide information on beneficiary registration, attendance, and performance. This information is also used by the TEC to monitor ITO performance.

Box 3.1 Boating industry investment plan

In New Zealand, the *Boating Industry Training Organization* is the ITO that represents the ship building industry, a sector highly intensive in specialized skilled labor, which, by its own calculations, will double over the next decade. It is also one of the manufacturing sectors that creates the most jobs in the country. The investment plan it submitted to obtain ITF funding for the 2008-2011 period can be consulted at http://rudderlive.nzmarine.com/bitodocs.asp .

First, the plan describes how the training strategy will meet government and sector priorities, as well as the commitments to execute the resources and performance indicators. Second, it makes explicit commitments to provide training, measured in terms of the STM units produced at each NZQF qualification level. Finally, it indicates the levels of private-sector cofinancing.

Added to this is a wealth of performance indicators, which are used to measure dimensions ranging from training efficiency to the participation of demographic minorities. These indicators include, for example, the program completion rate for apprentices, the number of credits obtained by each apprentice, and the rate of Maori women trained versus their rate of participation in the industry.

[3] The following formula is used to calculate the number of STMs to be financed:
STMs to be financed=number of individuals registered for the training* credits per individual per year /120

Direct funding scheme

The Government of New Zealand recently reviewed the ITF and found several areas with room for improvement. As a result, it proposed, first, to increase the degree of employer participation; second, to simplify the role of ITOs and improve their performance, since, according to the TEC analysis, many employers felt that ITO training initiatives did not address their needs; and finally, to increase competition among employers through direct funding.

The direct funding scheme (DFS) was created with these goals in mind. Its purpose was to provide employers with direct training alternatives and encourage ITOs to offer quality services. Since this was a new scheme, the government opted to conduct a limited pilot phase in 2014 and 2015 to permit adjustments in its implementation before expanding the program.

Under the DFS, funds are granted directly to businesses or business consortia that train at least 40 individuals per year. According to the TEC, this scheme would enable employers to design training plans more tailored to their needs, introduce innovative approaches, establish a direct dialogue with training providers, and lower transaction costs.

The funds can be used for different types of activities:

- To finance in-house training conducive to obtaining a qualification.
- To finance training outside the company.
- To finance mathematics and language training conducive to obtaining a qualification.

Only four businesses and/or consortia are currently participating in the pilot program. The four organizations were selected competitively. The selection panel consisted of two representatives from business and four from the TEC. According to the selection criteria:

- Businesses must have the resources to execute a successful program.
- They must have quality assurance strategies
- Credits and qualifications must be valid.

3.2 UNITED KINGDOM

a. Sector institutions

In the United Kingdom's lifelong learning system (Lifelong Learning UK), the principal financing entity is the Skills Funding Agency (SFA)**,** an executing agency of the Department for Business, Innovation & Skills (BIS), charged with:

- Providing financing to universities, private training organizations, and employers.
- Financing and coordinating learning programs.
- Administering loans for advanced learning offered directly to individuals (*24+ advanced learning loans*).

The SFA was created in 2010 to take over the functions of the Learning and Skills Council, which was abolished during a restructuring of the system. The SFA is designed to have representation of the private sector and the continuing education (known in the United Kingdom as "further education") sector. It has a 16-member advisory board, comprised of representatives from the continuing sector (through the training providers' association, for example), government entities (such as the BIS), and the private sector (such as McDonalds). The board meets five times a year and offers advice and feedback for policy-making.

Another important organization in the resource allocation process is the UK Commission for Employment and Skills (UKCES). Although the commission does not allocate resources directly, it plays a key role in the implementation of a new competitive fund, as we will see further on. The UKCES is a government-funded entity run by the private sector (with representatives of large and small business and unions) that provides support for sector policy design and is responsible for skills demand projections in the United Kingdom.

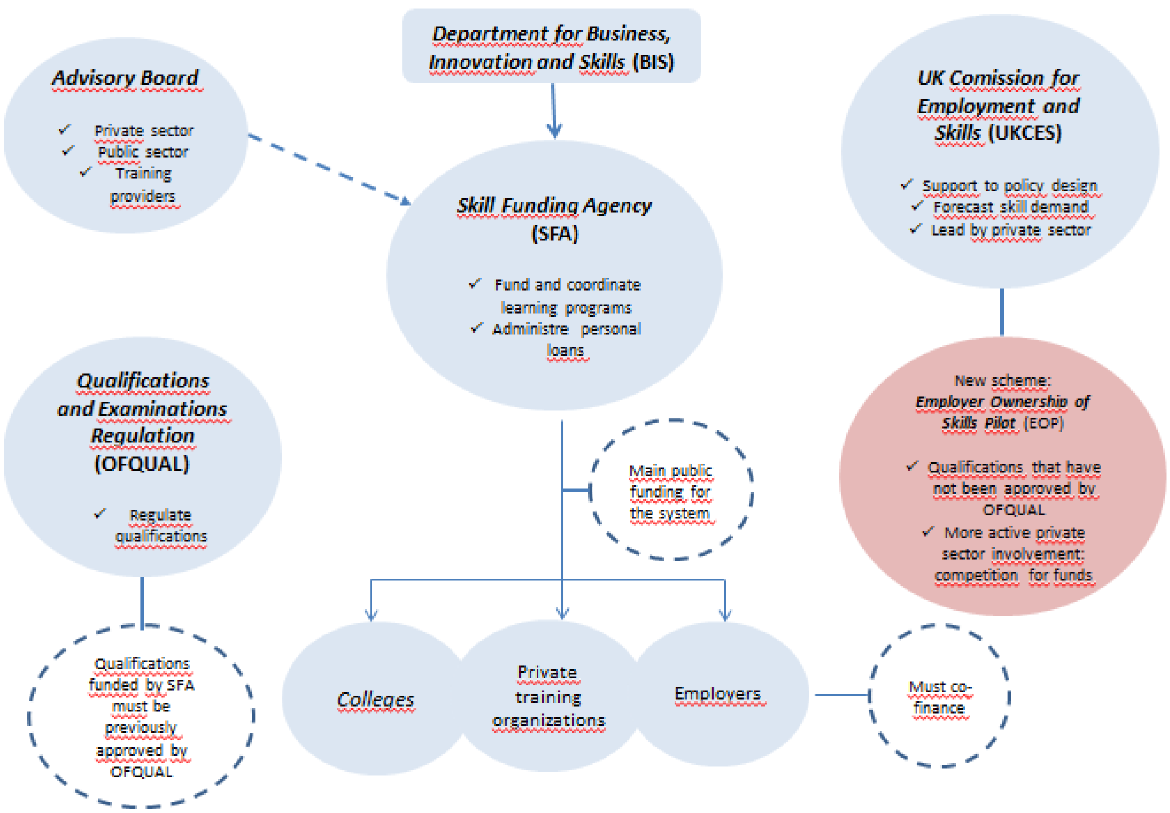
b. Public financing of training

The UK's vocational training system has a highly complex organizational and institutional structure with widely different funding schemes, the most important of which is the public SFA's line of funding for training providers.

Under this scheme, providers submit applications for funding based on the number of individuals receiving training to obtain qualifications. These individuals must be pre-approved by the Office of Qualifications and Examinations Regulation (Ofqual), the pertinent regulatory entity[4]. SFA awards funding on the basis of rates that depend on the number of individuals trained and a series of complex, detailed rules that indicate the courses that should be financed by the SFA and employers and the amount of cofinancing. The detailed nature of these rules makes the system very bureaucratic.

Since the system does not encourage a great deal of innovation, the SFA financing scheme also includes funds for training in certifications not yet approved by Ofqual. In this case, the provider must furnish evidence that the training is for certifications for which there is demand (Figure 3.2).

Figure 3.2 Financing for training in the United Kingdom



Source: Prepared by the authors

Up to now, the SFA funding process has involved very little private-sector participation. There is evidence that much of the training financed with public finds does not meet the

[4] Ofqual was created in 2010 to regulate qualifications and evaluations of vocational education. Under its regulations, qualifications should reliably reflect the knowledge and skills that students have demonstrated; there must also be a guarantee that the evaluation processes will be effective.

needs of employers. This is perhaps what explains the extremely high volume of vocational training that occurs outside the official qualifications system (CFE, 2012), which, in turn, has led to initiatives to increase private-sector participation. One of these is the Employer Ownership of Skills Pilot (EOP), a competitive fund for employers, which is described below.

c. *Employer Ownership of Skills Pilot (EOP)*

The EOP was a UKCES pilot program that began in 2012 and ended in 2014. Its objective was to achieve more active private-sector engagement in vocational education. To this end, it invited employers to compete for public funds to finance vocational education and job creation initiatives. Beyond being an alternative for the competitive allocation of public expenditure, the EOP was a vehicle for the UKCES to pursue a series of broader objectives. Specifically, it fostered a greater sense of ownership of the skills development agenda among employers, thereby contributing to more relevant, higher-quality vocational education.

EOP resources could be used to finance a wide range of activities not limited to training, which had to fall under the following categories:

- The development of current and future vocational skills (for example, investment in training, the development of new learning models, the design of new human resource management models, etc.).
- Industrial partnerships to assume greater responsibility in skills development in a region or sector – for example, through the creation of employer partnerships that would set the standards for learning and training programs, design vocational curricula for developing the talent needed by industry, and create peer review mechanisms to ensure the quality of in-house training.

A basic feature of this initiative is that it was a public-private cofinancing scheme. Every project was required to have counterpart financing from employers. In principle, this created greater incentives for them to submit relevant project proposals and intensify efforts to obtain good results through established monitoring and evaluation mechanisms.

An effort was made from the outset to ensure that the program was open to different projects and businesses. Thus, proposals did not need to include exhaustive information. However, all of them were required to contain the following: (i) a list of the results to be achieved and their expected impact; (ii) the rationale for the proposal and an explanation of why it could not be successfully implemented with alternative funding; (iii) the service delivery system; (iv) the level of employer investment; and (v) the level of public investment required.

The criteria for selecting the winning proposal included the following:

- **Employer ownership.** The nature and value of the employer's share of the investments had to be very clear; employers must have demonstrated that they had identified employment and skills development needs and that they would be managing the proposal.
- **Quality and rigor.** The proposals had to be rigorous and evidence-based and specify the quality assurance mechanisms.
- **Innovative approaches to skills and workforce development.** For example, innovative proposals in teaching or training contents were favored.
- **Impact and value for money.** Proposals were judged by the additional benefits that they yielded and whether they were proportional to the cost.
- **Feasibility**. The project had to be robust and demonstrate that all key stakeholders were actively committed.
- **Future prospects**. Here, the sustainability of the achievements was evaluated, along with whether the proposals offered value even beyond the life of the project.

These criteria were to be applied within the framework of sound institutional and management capacity, in which various entities and agencies monitored, inspected, and coordinated the activities. While it was in effect, the EOP completed two rounds of proposal financing. The government invested £34 million in the winners, and the companies contributed a total of £14.5 million in cash and another £16.5 million in kind. More than 600 companies participated directly in the design of proposals, and around 1,600 people benefited from the training programs.

At the close of the second phase of financing, positive results were observed in the following areas: (i) greater employer leadership, including active participation by senior executives in the strategic design of proposals and in dialogue with the government and other companies and/or industries; (ii) the emergence of economies of scale as a result of partnerships among enterprises that shared resources and diversified risks, a phenomenon that fostered the inclusion of smaller firms though greater integration of links in the production chain; (iii) incentives to increase training investment by employers as a result of government participation and support, motivating them to increase training expenditure (although the real increase in investment has yet to be evaluated); (iv) better targeting of investments through the design of training programs based on current and future skills needs; and (v) greater incentives for the design of innovative solutions, since the process led to the exploration of different training formats. This is what happened with the nuclear industry, which experimented with pre-employment training, and the automotive industry, which imported the BMW training model from Germany.

During the execution of the pilot program, room for improvement was found in the following areas: (i) given the problems recruiting youth between the ages of 16 and 18, an analysis of the necessary conditions for developing a pool of young talent was conducted, and middle schools were offered incentives to collaborate in the recruitment process; (ii) quality standards are critical to keep companies motivated to invest in training; (iii) the participation of smaller enterprises may be hindered by lack of access to financing; thus, when allocating funds, training programs should keep the different types of companies in mind; (iv) the production chain can be damaged if only large businesses benefit; thus, it is recommended that these enterprises partner with the smallest businesses, advising them and helping train their employees; and (v) the supply of highly skilled workers (who often come from an academic career path) is shrinking; hence, it will be necessary to develop accelerated learning processes and perhaps focus on the design of technical, instead of academic, curricula.

Box 3.2 EOP principles

With the EOP, the UKCES sought to introduce a radical change in the skills development agenda, shifting leadership from the public to the private sector.

This was a project with ambitious objectives that went far beyond the creation of a flexible public financing system for training. It listed five principles for the expected private sector participation in the skills development agenda:

1. **Employers should own the skills agenda.** The government provides the space for this to happen. It must also create the conditions for the best employers, working hand in hand with their employees, unions, training providers, and the education sector, to take charge and create opportunities for training, employment, and work experience.
2. **There should be a single market for skills development.** There are currently two markets: a public one that develops skills based on government priorities, and a private one responsive to business needs. These markets are not well-aligned.
3. **Skills development strategies should be designed by employer-led partnerships.** Employers are the ones who know what skills they need.
4. **Public contributions for vocational training should be shifted to employer incentives and investments.** Public spending should be shifted from a grants system to one that creates incentives and investments for employer-designed initiatives. That way, ownership and leadership remain in the hands of the private sector. An innovative credit and investment system should be developed that reaches a wide range of employers, large and small.
5. **Transactions should be transparent.** The current public financing system is excessively complex, preventing employers and individuals from understanding the government's contributions. Public financing should be simple and transparent, not bureaucratic. It should be designed to simplify employee and employer decisions to invest in training. The evaluation of public contributions should be based on employment and growth outcomes.

For more details, see the pilot launch document at:

https://www.gov.uk/government/uploads/system/uploads/attachment_data/file/306691/employer-ownership-of-skills-vision-report-final2.pdf

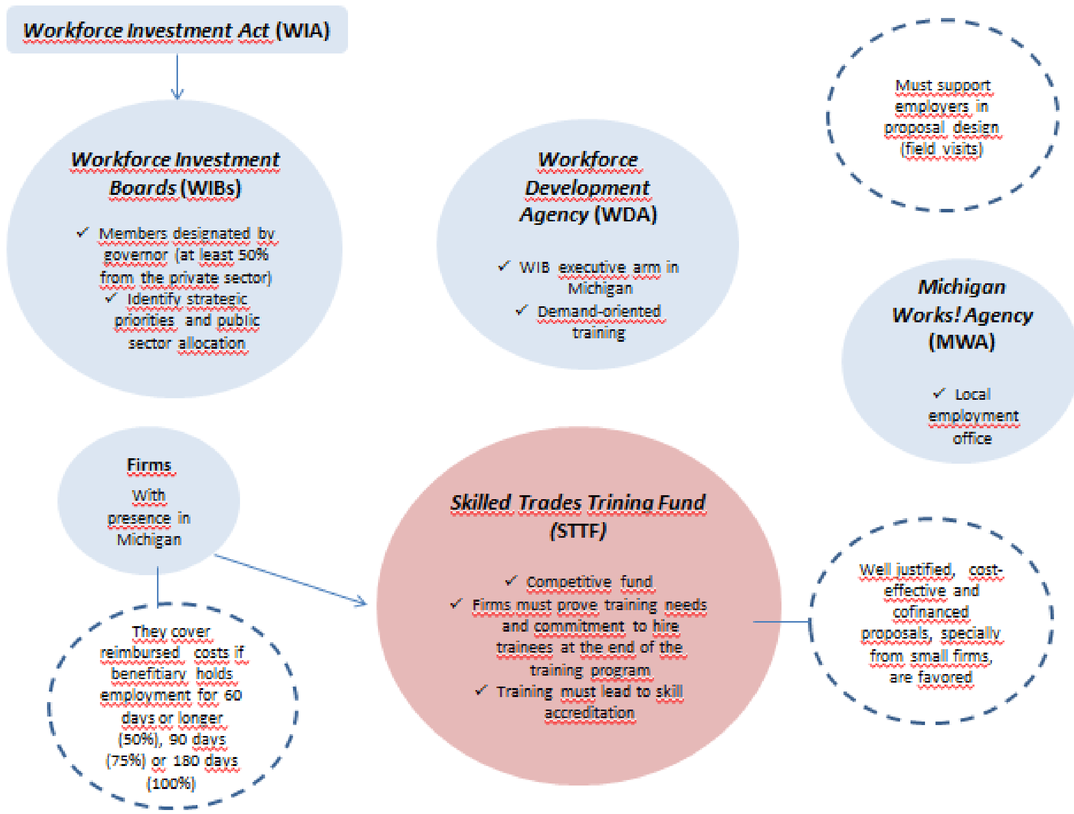
3.3 MICHIGAN (UNITED STATES)

a. *Sector institutions*

In the United States, state and local authorities play a very active role in the public financing of vocational training and workforce skills development. Since 1998, under the *Workforce Investment Act* (WIA), states were divided into one or more vocational training areas controlled by *Workforce Investment Boards* (WIB). WIBs are collegiate bodies whose members are appointed by the highest local authority elected by popular vote (for example, the mayor or governor). Under the law, at least 50% of WIB members must be representatives of the private sector. The main role of these boards is to set strategic priorities, identify industries with growth potential, and development investment plans, allocating a good part of the federal, state, and local public funds to vocational education programs. Thus, for example, all training programs created under the WIA (with the exception of the Job Corps) are administered by WIBs. The WIA gave WIBs the independence and flexibility to handle this responsibility, so their operations vary widely. The goal is to ensure that vocational education activities nimbly respond to the needs of the local productive sector

In the State of Michigan, the WIB is the *Governor's Talent Investment Board*, whose executive arm is the *Workforce Development Agency* (WDA). This agency has made progress toward a demand-driven training system one of its key priorities. Michigan's economy was hit hard by the Great Recession of 2008 and is still recovering from the drastic drop in employment. At the same time, businesses are having difficulty finding workers with the new skill sets they need. In light of this, the state's governor and legislature recommended the creation of the *Skilled Trades Training Fund* (STTF), a competitive fund created in 2013 to engage the productive sector in the design of demand-driven training initiatives. In 2016, the average award to each project approved was US$38,000 (Figure 3.3).

Figure 3.3 Financing of training in the State of Michigan, United States



Source: Prepared by authors

b. *Skilled Trades Training Fund (STTF)*

The Skilled Trades Training Fund competitively awards resources for the development and implementation of demand-driven training initiatives. Resources are awarded to businesses that can prove a training need and design a training program in partnership with a local office of the *Michigan Works! Agency* (MWA).

Employers wishing to participate in the fund must: (i) be located in Michigan; (ii) demonstrate the need for training that will enable the company to compete and grow; (iii) commit to hiring the participants at the end of the course or training activity, paying them wages equal to or higher than those in the market; and (iv) guarantee that the training will lead to accreditation in a skill that is transferable to other employees in the same industry. The goal is for accreditation to enable an individual to find or retain a job (for example, a certificate in welding). The STTF cannot be used to finance training in soft skills, languages, or leadership.

The funds are used to finance short-term training activities (three months or less, except in the case of apprentices) that enable the current training needs of employers to be met. Some examples of the types of training that would be financed are: classroom training, on-site training for the individuals to be hired, and apprenticeship contracts. The STTF stipulates the maximum funding for training (US$1,500 per trainee and, in the case of apprentices, US$3,000). Employers initially assume the cost, 50% of which will be reimbursed once the trainee has retained employment for 60 days following training completion; 75% when employment is retained for 90 days; and 100 % when employment is retained for 180 days.

The local employment agency, MWA, must help employers prepare their proposals. In practice, MWA staff make field visits to help them devise skills development strategies that include:

- Human resource recruitment plans
- Personnel selection strategies
- Hiring incentives
- Training for new and current employees
- Alternative sources of funding to train personnel (including tax incentives)
- The identification of training providers

Selection of the winning companies is based on a scoring system that awards different dimensions. Priority is given to proposals that are better justified, more economical and expeditious, cofinanced with other sources, and submitted by small firms. The selection criteria include:

- Rationale: business case for training
- Employer contribution (leveraged funds)
- Cost per trainee
- Use of complementary funds
- Timeliness (training begins four to six weeks after application)
- Start date and length of training
- Size of the firm (higher score if it has fewer than 50 employees)
- The training leads to an accreditation

3.4 BARBADOS

a. *Sector institutions*

The Ministry of Labour, Social Security & Human Resources Development is responsible for active labor market policies, including intermediation and training services. This ministry's mandate is to supervise the *Technical and Vocational Education and Training Council* (TVET Council), which sets the standards for certification and accreditation and finances training, and the Barbados Vocational Training Board (BVTB), which provides specialized training. In 1993, the *Vocational Education and Training Act* was passed, giving the TVET Council the functions of: (i) advising the Ministry of Labour in technical and vocational education and training matters; (ii) coordinating the vocational education system; (iii) administering the *Employment and Training Fund* (ETF); (iv) setting occupational standards for technical and vocational education; (v) setting priorities in the areas of skills, qualifications, and accreditation development; and; (vi) issuing national and regional certifications (*National Vocational Qualifications* (NVQ) and *Caribbean Vocational Qualifications* (CVQ), respectively).

The ETF grants funds to employers, training institutions, and employer or worker associations to promote vocational training in technical areas. It is financed from a payroll tax. The target population of the ETF consists of currently employed or unemployed people seeking reemployment or to join the labor force for the first time. Financing is provided as long as it meets the needs of strategic economic sectors, and employers must cover 25% of the cost of the training. The ETF recently has introduced many changes based on the experiences made of the Competency Based Training fund.

b. Competency-based Training Fund (CBTF)

In Barbados, there is considerable evidence of a gap between the supply and demand for skills (Ministry of Education and Human Resource Development and Ministry of Labour and Social Development, 2011). Therefore, in 2011, the Government of Barbados, with support from the European Union, began implementing a five-year human resource development strategy, the Barbados Human Resource Development Strategy, to provide a framework for strengthening the vocational education system to boost productivity and competitiveness while promoting sustainable economic growth.

To this end, the Government of Barbados, through the TVET Council, launched a pilot initiative as part of the Skills for the Future program (IDB BA-L1016) to finance the design and implementation of demand-driven training proposals through the implementation of a competitive fund, the *Competency-based Training Fund* (CBTF). Established in 2013, the fund operates through tenders for the selection of proposals that must: (i) be in to a productive sector prioritized in the country's development strategy; (ii) adhere to the occupational standards set by the TVET Council, based on the National/Caribbean Vocational Qualifications (NVQ/CVQ); (iii) culminate in certification; and (iv) be submitted by a partnership of at least one employer and one training provider or groups thereof.

Proposals are evaluated by a six-member committee consisting of representatives of employers, training institutions, unions, the Ministry of Education, Science, Technology, and Innovation (METI), and the TVET Council. The following elements are reviewed: (i) a description of the problem and proposed training program; (ii) the specific objective and target group; (iii) an operational description of the program; (iv) institutional schemes; (v) costs and budget; and (vi) monitoring indicators. Trainees can be people who are currently employed or potential employees.

The CBTF has now completed four proposal cycles and financed 30 training projects in 16 economic sectors for 4,160 persons to benefit from the training. Successful partnerships can receive financing for 100% of their proposal, as long as the figure does not exceed $BBD 500,000 (US$250,000), and have on average 18 months to implement their proposal. CBTF funding currently comes from an IDB loan (BA-L1016 *Skills for the Future*), but as of November 2018, it will be financed by the *Employment and Training Fund* (ETF), which has started to integrate some of the project's good practices from the *CBTF* to the traditional fund including the requirement of certification at program conclusion, closer monitoring of the implementation of proposals, and the preference to have partnerships between employers and training institutions apply for the fund..

The positive experience of Barbados has served as a model for new initiatives in the Caribbean. The Bahamas and Trinidad and Tobago (Boxes 3.3 and 3.4) have new projects promoted by the IDB that, like the CBTF, seek to align the supply of skills with the demand of the productive sector through direct employer involvement. Alignment with development goals is also essential.

Box 3.3 Matching Grant Facility (MGF) of Bahamas

The Government of The Bahamas, with IDB support, has launched an apprenticeship program with the object of reducing youth unemployment, better aligning the supply and demand for skills, and forging close ties between the productive sector and training institutions. It will also create sector skills councils in three strategic sectors to facilitate the identification of priority skills and the development of occupational and training curriculum standards and establish related quality assurance standards and processes. The choice of sectors will be based on an estimate of future vacancies and growth potential.

In order to establish a cofinancing mechanism for the apprenticeship program, a Matching Grant Facility (MGF) will be set up to ensure a transparent financing scheme that quickly responds to the demand for skills in the productive sector and has credibility among employers.

Businesses interested in applying to the MGF must submit proposals for vocational education programs that are part of an apprenticeship scheme. Each proposal must include a training plan, designed by either a training entity, a sector skills council, or the company itself, although in this latter case the rationale must be more exhaustive. Training proposals must always meet the quality standards of the sector skills councils and culminate with the issue of a certification recognized by the industry. Businesses will also be required to report on progress, the drop-out rate, and the general status of the project in order to receive funds, which will be transferred every three or six months, as stipulated on approval of the proposal to be financed.

This mechanism for competitively awarding funds will enable the government to create a platform for businesses from the preselected sectors to submit their apprentice training proposals and indicate their contribution to covering the associated costs. The MGF is a mechanism with operational capacity at two levels: (i) receiving and evaluating the proposals submitted by businesses, and (ii) defining and executing the flow of disbursements issued by the government and businesses for training purposes, which will be contingent on a skills assessment of the apprentices. In the strategic sphere, the MGF will identify the specific training needs of the industry and the options among institutional training providers that meet industry requirements.

Box 3.4. Trinidad and Tobago: Skills for Global Services Initiative

Trinidad and Tobago's economy is highly dependent on the oil and gas sector, and the country has long tried to promote a diversification agenda. To this end, it has identified a series of strategic sectors toward which it can diversify its economy -- one of them being IT-enabled services (ITES). Although the country has a number of comparative advantages for developing this area (a highly educated English-speaking population, a convenient time zone, and good infrastructure), it still lacks the specialized human capital to do so. In this context, in 2017, the Ministry of Planning and Development, with IDB support, launched a pilot competitive fund called Skills for Global Services (SGS) to finance training proposals in the ITES sector. This initiative is part of a comprehensive productive development program to promote ITES through other action to complement skills development, such as foreign investment and regulatory changes.

Through the SGS, financing is competitively awarded for skills development. A call has been issued to companies in the ITES sector to partner with training entities or academic institutions to submit skills development proposals that include activities such as training, certification, and curriculum development. The idea is: (i) to promote better alignment between the supply and demand for workforce skills; (ii) to design a process for encouraging dialogue between companies and training institutions in which employers participate in the design of curricula and training programs; (iii) to give workers certifiable competencies with a seal of quality to facilitate their professional development; and (iv) to create a simple, transparent, and participatory financing mechanism.

The SGS can finance a wide array of proposals, including social and emotional skills training. However, proposals must have contents geared to developing technical skills in information technology. The training must also lead to nationally or internationally recognized certifications. While the fund requires participating businesses to be registered in Trinidad and Tobago, training providers may be international. The initiative also offers opportunities for technical assistance, in which expert consultants help participants in the fund draft their proposals. These are voluntary activities in which employers receive guidance in determining the best way to use resources and prepare proposals accordingly.

Once the application period has ended, a selection committee comprised of representatives of the productive, public, and training sectors evaluates them and decides which proposals will receive financing, based on pre-set criteria, namely: (i) the importance of the proposal to expanding the ITES sector; (ii) alignment between the identified skills demand and the proposed solution; (iii) the universe of beneficiaries, (iv) the ability to evaluate the proposal through performance indicators; (v) future sustainability, etc. There will be multiple winners, which can receive up to USD 70,000 per proposal. The process will be monitored and evaluated by an independent committee during the implementation period.

4. Final comments and conclusions

This Technical Note has discussed the utility of competitive funds as an instrument for better allocating resources in the vocational education market and incentivizing quality and relevance in training and public-private cofinancing. It has also presented a variety of competitive fund schemes found in countries at the forefront of vocational training. While the examples of New Zealand, the United Kingdom, Michigan (USA), and Barbados have elements in common, they also differ in key areas. They are worth studying so that lessons applicable to Latin America and the Caribbean can be drawn to develop innovative public financing for training.

In the case of New Zealand, a country with a long tradition of results-based financing, funds are adjudicated on the basis of specific targets set for a wide range of performance indicators. Moreover, proposals in that country must be aligned with the national development strategy, reflecting the fact that skills development must be strategically aligned with the country's national economic development program.

In the case of the UK's EOP, the emphasis was on flexibility in the use of resources and the targets to be monitored, reflecting the fact that the EOP's ultimate goal was for the private sector to assume greater leadership in the skills development agenda. The program was based on the principle that employers are the ones most capable of determining the best use of resources, and consistent with that objective, the fund was designed to permit the resources to be invested in a wide range of options.

This principle is shared by the Barbados' CTBF, a fund that also stresses private-sector leadership in the preparation of training proposals. Notwithstanding, its design is also geared to increasing the supply of training that is competency-based training and leads to certification. The fund also has the clear objective of furthering partnerships between employers and the training sector.

The flexibility of the UK's EOP and Barbados' CTBF stands in contrast to Michigan's STTF, a fund whose clear and specific objective is to revive the local labor market in the wake of the 2008 recession. While the STTF encourages active private-sector participation, the activities that employers can finance with these resources are tightly restricted to short-term training.

The pilot programs of The Bahamas and Trinidad and Tobago also differ in important ways. The MFG of The Bahamas is part of a strategy to promote a specific training modality: in-house youth apprenticeship programs. The SGS in Trinidad and Tobago, in contrast, can finance a rather wide range of skills development proposals. It can even finance curriculum development and certification. It is a skills development proposal born of a comprehensive productive development policy. Its focus is therefore on a strategic sector of the national diversification agenda.

These examples illustrate how the design of competitive funds can vary with policy objectives. However, some common elements are worth highlighting. First, the intent to actively engage the private sector is a constant. In the case of the UK's EOP, the fund was explicitly created to replace the standard scheme in which training is financed by the public sector. In the case of New Zealand, the direct funding scheme grew out of a strategy to forge a direct link with the private sector, since under the traditional scheme, financing was channeled through industry associations. In Michigan, the STTF was created as a subsidy for demand-driven training.

Second, in many cases, the intent was to channel resources to strategic sectors. This poses an operational challenge for administering the fund, because the committee that adjudicates the resources must have sufficient criteria and knowledge of the local economy and competing industries. This is facilitated in New Zealand by a national skills development strategy. The eligibility criteria In Trinidad and Tobago limit the fund to a sector previously designated a priority by the national government

Third, the criteria for awarding these funds reward—or require, as in the case of the MGF in The Bahamas—activities that are cofinanced with resources from the business, or in some cases, the workers. This could at least partially mitigate a common risk in public training subsidies: deadweight loss, a phenomenon that occurs when public resources are used to finance training activities that would have taken place in any event. Even so, it is a latent risk that must be considered in the design and adjudication of the funds and can be measured with rigorous impact assessments.

Finally – and this is fundamental for designing better options for LAC – while the funds are part of different institutional frameworks, their design includes management mechanisms to ensure efficient, transparent, and result-based use of the public funds allocated to vocational education

The use of competitive funds to finance vocational education is still rather uncommon in the LAC countries. Progress in their implementation would require substantial resources. Implementing competitive funds requires considerable technical and managerial capacity in both the public and private sector. Nevertheless, the innovative experiences with the three projects in the Caribbean indicates that this is a promising approach that can yield substantial gains, permit transparent and efficient resource allocation, and connect the productive sector with training providers – all of which are essential to any successful vocational education policy.

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