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Praxis

Encouraging small firms to invest in training: learning from overseas

Professor Ian Stone

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Praxis Points

Policy implications: areas for further discussion

This edition of Praxis raises a number of questions. For example, can the way in which policy levers, used overseas to encourage small firms to invest in training, be assessed in terms of their suitability in a UK context? Other questions include:

1. Skills formation activities in small firms are often informal. How can recognition for informal training activities be improved?

2. How can employer networks and supply chains be harnessed to support training?

3. In what ways are the UK's 'voluntarist' traditions likely to make certain policy options more effective than others in positively affecting the training behaviour of small employers?

4. Of the various policy levers used to influence training by small firms, how can selected interventions be combined for best overall effect in the UK context?

5. Low-skilled and low-qualified workers in small firms are particularly disadvantaged when it comes to training, as it is often better educated workers that access skills development opportunities. How can these policy levers be designed to benefit a broader range of workers?

6. Are there practical and effective means of developing demand for training in smaller firms which link skill formation with the enhancement of ambition regarding product or service quality?

7. Which of the policy levers are appropriate in the context of public finance constraints?

Engage with the debate
The aim of Praxis is to stimulate discussion and debate on employment and skills policy issues and we encourage readers to engage with the questions raised above, or make any additional points in response to this paper, on the Praxis pages of the UKCES website (http://www.ukces.org.uk/our-work/research-and-policy/praxis/).

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The views expressed in Praxis are those of the authors and do not necessarily represent those of the UK Commission for Employment and Skills.

Foreword

Welcome to Praxis, the UK Commission for Employment and Skills' policy think piece series, which seeks to highlight key and emerging issues in employment and skills policy for discussion and debate.

More adults engage in learning at work than anywhere else, and given that businesses with fewer than 25 workers account for over 90% of all employers in the UK, both the quantity and quality of the training available is of critical importance.

In this edition of Praxis, Ian Stone identifies and explores the main barriers to training experienced by small firms and, drawing on the experiences of international competitors and comparator nations, considers possible policy responses and interventions.

Professor Stone's work[1] raises some important questions for UK skills policy in relation to smaller firms. He questions whether the UK's 'voluntarist' tradition mean that policy levers successfully implemented elsewhere would have less impact in the UK. He also challenges the framing of the 'problem' of training in small firms as simply an issue of overcoming supply-related barriers. Instead he explores whether policy can be used to raise demand for skills formation, by linking it to increased ambition for high value products or services.

These questions must of course be answered with consideration of the political and economic context in which future policy will be developed. The reality of long term fiscal constraints will impact on the type and reach of policy interventions available to support smaller firms. However, given the important role of skills in building stronger, more competitive businesses, the challenges raised by this paper are of critical importance in ensuring that small firms can maximise the opportunities created by economic recovery.

[1] *This paper draws from research conducted for the SSDA, including a study (with Paul Braidford) published as SSDA Research Report 30 (March 2008) Engaging Small employers in continuing Training: An International Review of Policies and Initiatives (available on UKCES website http://www.ukces.org.uk/upload/pdf/summary_30_1.pdf).*

The UK Commission is currently engaged in a transnational programme of activity with the OECD that seeks to identify ways of overcoming barriers to workforce development in small and medium enterprises (SMEs). The study is collecting evidence at a local and regional level on SMEs and their training activities in a number of OECD countries (including the UK) and will report in summer 2010. We hope that, alongside this edition of Praxis, this work will contribute to a wider debate about policy responses to the specific skills needs of small firms.

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About the author

Ian Stone is an economist and professorial fellow in Durham Business School and St Chad's College, Durham University, where he is joint director of the Policy Research Group. As a Research Fellow for the UK Commission for Employment and Skills, he supported the programme of work on collective measures. Ian has undertaken numerous studies of labour markets and skill formation at the regional scale, and in respect to small businesses – including one for the DTI's Small Business Service and Small Business Council on high performance working in small firms. He has been adviser to ONE North East, North East Regional Assembly, BERR, UK Cabinet Office and ESRC, and also a member of the SSDA Expert Advisory Panel. He regularly provides training to officials of the European Commission (Employment Directorate), and was an invited expert on a recent EC delegation to Chile.

"Ultimately, a policy outcome might be judged successful if it raises the general level of skills – and thus also the incomes of employers and employees – to a greater extent than the policy cost"

1. Engaging small employers in training – a key challenge

Small firms and the UK skills policy agenda

The workplace is where most adults learn, and with businesses with fewer than 25 workers accounting for over 90% of all employers, the extent and quality of training undertaken by small firms is thus important. Moreover, firms that train their workers are significantly less likely to close than those that do not. It is a matter of policy concern, therefore, that, on various measures of the activity, the smaller the firm the less likely it is to be engaged in training, and that 36% of UK small firms undertake no training at all.

In-house, informal training is preferred by smaller employers, primarily because it can be tailored to their needs and conducted at suitable times. However, Johnson (2002) shows that, while allowing for both on- and off-the-job training narrows the gap somewhat, employers with 100+ workers are still nearly twice as likely to train compared to those with fewer than five employees. Small firms often disregard the role of skills in the overall business planning process. Only 30% of small employers – mainly the more innovative ones – measure the effects of training, including its contribution to financial performance, or view qualifications favourably. Fully one-half of small firms perceive no need for further training of their workforce.

One explanation for these patterns is that training costs per employee are higher for smaller firms, reflecting its disruption to their operations and their lack of access to economies of scale. Such practicalities mean that the problem is not confined to the UK. Thus, a 2005 EU study concluded that continuing vocational training (CVT) was the 'weakest link' in the lifelong learning chain: enterprises with 10-19 employees spent only 1.5% of labour costs on CVT, compared to the average of 2.3%. Just one-third of Australian small firms provide structured training for employees compared with 70% and 98% respectively for medium and large enterprises. Canadian establishments of 500 or more employees have a participation rate (formal training) of 37% – double that of firms with fewer than 20 workers.

Yet most research on engaging employers in training has neglected to address adequately the distinct situation of small employers. Thus, in the context of attempts, following the *Leitch Review of Skills*, to increase UK employer investment in training, this paper identifies the main barriers to training faced by small firms and considers possible policy responses. Drawing upon experience overseas, it discusses interventions that might improve training performance through addressing the specific circumstances and needs of small firms.

2. What stops small firms investing in their workforce?

Barriers to training

Small businesses consistently identify more barriers to training than larger firms. The main obstacles, according to empirical research, are that:

- Small employers commonly lack information on what training is available to them, as well as evidence of the benefits of training to set against perceived and real barriers to training activity
- Even where they perceive training to be of value, releasing employees for (especially formal) training is more difficult for smaller employers. Lost working time is an especially important constraint with respect to owner-manager training
- Small firms often report difficulty accessing training tailored to their needs in terms of type and quality, scheduling, location etc. Providers can be reluctant to supply to small businesses, given costs of organising and customising the training, the often small numbers of trainees, and employer reticence with respect to paying the full cost
- Many owner-managers consider that undergoing training themselves will not enhance their ability to operate the firm, although fear of exposing deficiencies in their knowledge is sometimes behind their reluctance to participate
- Poaching of skilled workers by other firms and training leading to wage demands, are frequently identified as obstacles. Larger firms often pay higher wage rates, so formal qualifications are perceived by many small employers as more valuable to employees than the business itself. Thus, many provide only in-house firm-specific training, which produces skills that are less transferable in the open market
- Lack of access to economies of scale in training raises training costs for smaller employers, who, compared to large firms, pay typically three times more per member of staff undergoing formal training.

This can be seen as a prime example of market failure. **Market failure** refers to dimensions of the labour market's operation that can cause it to produce a sub-optimal outcome – most seriously, from both an employer's and national economic perspective, an under-supply of the skills needed to produce higher quality goods and/or achieve higher productivity. Various elements identified in the above list of obstacles are consistent with mechanisms associated with market failure:

- Information deficiencies – lack of knowledge of what training is available and how it might benefit the business influences employer decisions on investment in skill formation
- Short-termism and risk aversion – small firms tend to be more oriented to immediate goals, notably survival, and operate to shorter horizons than larger ones; opportunity costs are higher for formal training and informal methods allow firms to meet immediate business imperatives
- Externalities – benefits to workforce skilling are not confined to the small employer investing in training because of 'spillovers'; part of the gains can go to individual employees (higher wages), the state (taxation) and other employers ('free riders' who 'poach' workers from other firms by offering higher wages, rather than train their own). This reduces the employer's incentive to train and induces patterns of training designed to minimise such losses
- Capital market imperfections – the relatively high financial costs of training for small firms are exacerbated by the fact that the direct collateral to secure borrowing to invest in training – the individual employee – is mobile between firms.

Where the level (and type) of training investment is restrained by market failure, it is widely held that **intervention is justified**. Thus, bringing about conditions that reduce poaching by other firms may encourage small firms to train. Similarly, improved information on available training, more relevant and accessible training programmes, and demonstrating positive impacts upon business performance, can also be expected to raise training levels.

It is also widely recognised that suppressed demand for training among small employers arises because of a further 'system' failure – the low skills equilibrium. This ultimately derives from product market strategies emphasising low specification products or services, produced by low skilled workers. Market demand, production strategies and skill levels become locked into a path dependent, self-reinforcing cycle. Limited employer demand for skills lowers uptake of learning opportunities; the impact upon skills supply, in turn, discourages employers from choosing production methods that emphasise skills. Surveys show that the weakest training performances tend to occur among small employers in such contexts, and where such firms are dominant, this can translate to sub-optimal performance of whole sectors.

Small employers with more ambitious strategies – based on innovation, growth and higher value production – engage more intensively in training, in spite of the constraints. Providing the incentives and conditions that encourage firms on this path can be expected to raise the optimum level of demand for skills among employers so as to meet the needs of more sophisticated systems of production.

The policy challenge

The operating environment faced by small businesses, and related barriers, makes it likely that training in such firms is below an 'optimal' level. However, it should not be assumed that optimality (i.e. an economically efficient level of training) can be equated with achieving parity with larger firms in terms of standard training measures. While informal training is often more relevant to smaller companies, formal training is easier to measure and tends to dominate comparative statistics. Simply increasing the latter form of training, in a small firm context, may contribute more to improving efficiency in the broader labour market than in the firm itself.

It is widely accepted that employer investment in training tends often to be below the 'optimum' level, both in a static sense (resulting from market failure) and dynamic context (low aspirations regarding production strategies). In both respects, there are solid grounds for anticipating that this will apply to a greater extent to small firms than large ones. The policy challenge, in raising levels of skill formation among small employers, is thus one of finding mechanisms that address the static or/and dynamic influences. Ultimately, a policy outcome might be judged successful if it raises the general level of skills – and thus also the incomes of employers and employees – to a greater extent than the policy cost (allowing for taxation). The situation can thus be improved without actually achieving the 'optimum' position. Ideally, policy should encourage a dynamic effect that both demands and gives rise to higher skills investment.

3. What can government do?

Key areas for action

[2] e.g. Dawe and Nguyen 2007

Reviews of policy for addressing obstacles to small employer training in different countries[2], suggest the need to focus on the following key areas:

- Present 'the business case' to small firms, to change prevailing perceptions/culture, including the desirability of skills-intensive production and workplace development strategies
- Organise effective sectoral/regional outreach mechanisms for directly dealing with small business owner-managers, providing them with information and support (including HR support) and identifying ongoing training appropriate to their evolving business needs
- Ensure there is flexible provision which individualises training information, content and delivery to the needs of each small business (including management training)
- Integrate formal training and learning with informal learning processes in the workplace, accommodating training around work demands and minimising time spent off-site
- Reduce training costs through financial incentives, e.g. through subsidies and tax concessions, targeted on small firms and existing workers
- Collaboration between small businesses through pooling resources and networking (and, more broadly, to provide opportunities for small businesses to share skills, knowledge and experience with other business people)
- Develop training partnerships between larger firms and small businesses
- Ensure that facilitators and trainers have the appropriate networks, motivation and experience to enable them to be trusted and respected by all business participants.

An international review of intervention measures

Changing employer outlook

Making 'the business case for training' – based on empirical evidence on the links between skills and business performance – is widely recognised as a potential means of developing interest in skills formation among small firms. However, Nordic countries have piloted approaches that encourage training as part of a broader attempt to improve competitiveness through strengthening workplaces and improving work experience. They seek to change the outlook of small firms generally towards a more holistic appreciation of the performance advantages of organisational development, and the integral place of training within this process.

Finland's *New Workplace Development Programme* (NWDP), for example, provides small and medium sized enterprises (SMEs) with funding for workplace analysis, project planning, learning networks, and dissemination of lessons. Training is integral to this, but is placed in its organisational context, and both the quality and equality of access to learning opportunities are emphasised. The NWDP sits alongside other programmes that help integrate skills acquisition and improvements in workforce wellbeing and productivity – at a broader scale framed by Finland's national innovation strategy, which is designed to accommodate the needs of small businesses.

Similar policy approaches oriented towards SMEs, both with respect to workplace development and innovation, are embodied in Norway's *Competence Reform*. This seeks to move beyond simply increasing the supply of skills, towards *deploying* them for purposes of innovation and value creation. Hence, there is much interest in linking human capital/knowledge assets to future earnings prospects and business value, and in approaching the quality of working life as a *driver* of training changes. As in Finland, there is emphasis upon quality of workplace training and more equal access to it.

Information and guidance

Lack of capacity for human resource development within smaller firms inhibits their engagement in training. This can be addressed through regular interactions with agents or brokers, or by actually establishing in-house HR management capacity. South Africa's 1% national training levy, which embraces many micro firms, operates to encourage the development of such capacity. Part of the levy can only be re-claimed by enterprises if they have appointed a Skills Development Facilitator – either an externally-appointed consultant, or someone assigned the duty internally – to help enterprises develop an annual skills plan and to inform employers of developments relating to accreditation, available courses etc.

Canada's Sector Councils recognise the need for outreach activities to small employers, to deliver HR-related information and advice to small businesses. Training advisors bring 'training conversations' to workplaces in small firm dominated sectors (e.g. plastics), as part of an extensive programme of visits to learn about employers' business and skills requirements, establish ongoing relationships, and communicate how to access web-based and other services. An average of 6-7 visits is commonly found to be needed, indicating that this a resource-intensive approach.

Forms of training

Training needs of small firms differ from those of larger firms, making design of training and qualifications an important factor in engaging small firms. Training needs to be demand driven, targeted on real needs and specific working environments. Flexibility in delivery systems is crucial – specifically the need for unit-based, 'bite-sized' qualifications compatible with the workplace.

Belgium's training vouchers scheme, targeted upon small (and especially micro) firms, accommodates these needs. Vouchers purchased on-line (matched by government up to a €6000 maximum) are used by employers to purchase training from accredited providers.

Both company-specific and general training is eligible, encouraging a wide range of training. Indeed, the scheme has encouraged providers to design courses specifically for small businesses. Although popular for being non-bureaucratic and simple to use, the system is criticised for having substantial deadweight costs.

Sweden's Lifelong Learning Project is a pilot scheme that integrates workforce skills-upgrading within a continuous learning framework. This is held to appeal especially to smaller employers because of its primary focus upon meeting their skill development needs rather than achieving formal qualifications. New Zealand's qualifications framework appears successfully to facilitate the bespoke design of qualifications, allowing mixing and matching of course units tailored towards small businesses or sector-specific knowledge.
Industry qualifications can consist of both generic and specific units – e.g. the commercial road transport certificate includes maintaining personal presentation and communication skills alongside credits for knowledge of traffic law and executing vehicle manoeuvres. Small firms have welcomed the framework for flexibility of content, emphasis on small units of assessment, and relevance to different sectors.

Management training

Owner-managers of small firms are found generally to prefer mentoring and longer-term business development programmes, with intensive training and support sessions at intervals over a period of months or years. Their engagement in training is promoted where the learner studies and critically reflects on their own actions and experiences. Embedding this reflective learning within social and business networks is considered to enhance its effectiveness. Successful examples of management training initiatives overseas often stress, in addition, the unequivocal benefits for the participant's business post-training, including:

- gaining access to a larger firm's supply chain or network (e.g. the Belgian Strategic Plan Kempen (see below)
- developing management skills at the same time as encouraging networking within a cluster (e.g. Ireland's FAS Development Cluster)
- solving actual business challenges using experienced mentors (e.g. the Dutch Stichting Ondernemersklankbord initiative), or certificate-based training focusing on the manager's own business (e.g. Finland's Specialist Management Training scheme); and
- achieving business insights, such as in France's Re-Créer programme, where entrepreneurs who have experienced a business crisis communicate the lessons to others.

Tax incentives

Most countries permit firms to offset training costs against profits in their tax returns, some even allowing deductions greater than the costs incurred. Such schemes are easy to apply, inexpensive to administer, allow employers to decide who will be trained (and how), and shift the incentive balance towards training rather than recruiting skills externally. Careful design of the tax arrangements can specifically incentivise small employers to invest in training and reduce the level of deadweight costs. The Netherlands, for example, recently experimented with an extra deduction from taxable profits on training expenditures, plus an additional deduction for firms spending less than a specified amount. In targeting firms with low absolute levels of training expenditure, the incentive both automatically targeted small firms and minimised deadweight losses.

Malta has developed perhaps the most elaborate and highly targeted tax-related scheme, where eligibility for deduction is focused on training of full-time employees in particular sectors. The rate of reimbursement is higher for small than large enterprises, and respectively higher still if the training is generic rather than workplace-specific.

France, too, has long operated training tax credit for those SMEs that, year after year, invest in vocational training beyond the statutory obligation, with a higher credit for firms with fewer than 50 employees.

Through being related to the previous year's training, the device is an incentive for increasing training expenditure and restricts deadweight expenditure. Belgium's (Flemish) Vlamivorm project, offering a reduction of property tax equivalent to spending on worker training, also achieved good results without undue deadweight cost through targeting sectors with a poor training record. It also achieved very high participation of micro firms, by making internally-organised informal training eligible for the reduction.

Although targeting – for example through differential rates based on firm size – can lower deadweight expenditure, it usually also leads to higher administration costs for tax authorities and employers. The burden of 'form-filling', together with various other barriers, may explain why substantial fiscal incentives are needed to activate small employers. Tax incentives appear to have had little impact on smaller firms in South Korea during the 1990s, despite re-imbursement levels that were three times the actual outlay on training fees (and three times higher than for larger firms).

Training subsidies

Small firms are also frequently a target for training subsidies. An example is Belgium's voucher scheme (discussed above). Another is in France, where a subsidy of up to 70% of training costs is offered, with a further 10% for special groups of employees. Targeting is effective: 90% of beneficiaries have fewer than 50 employees. Evaluation suggests that training in small firms is relatively sensitive to the availability of subsidies – its incidence rose significantly in those enterprises assisted – where both qualified and unqualified workers were found to have received training.

Typically, subsidy support schemes are related only weakly to business performance, although some schemes seek to achieve a closer connection between the two. Ireland's Training Support Scheme purposely restricts subsidies to training activities explicitly linked to business strategy, while SME training support for R&D projects in Flanders, Belgium, offers an example of how staff development subsidies can support innovation projects.

Pay-back contracts

Contract arrangements are sometimes made to permit employers to recover at least part of their investment in training staff members in the event that they leave voluntarily soon afterwards. Through reducing the risks involved, this encourages employers to support training. While such arrangements are in rare cases enshrined in law, they are relatively common in individual contracts and collective agreements. In Germany, they are found to operate in perhaps 15% of firms – and proportionately more in Switzerland – but no example is found of the mechanism targeted on small firms specifically or specifically adapted to their needs.

Training levies

Levy schemes are common – a recent EU review found that they accounted for one in ten demand-oriented instruments for fostering workforce training. There are two main kinds: (1) 'train-or-pay' systems requiring employers to invest a particular amount (a share of payroll) on training, or pay a tax based on the shortfall; and (2) employer contributions to a common fund (administered nationally or through a sector body), from which training costs are met. Such schemes can result in higher levels of employer-based training, while addressing 'poaching' by requiring all firms to contribute to training expenditures. They also offer considerable scope for facilitating training among small employers through earmarking funds.

Some schemes are criticised, however, for encouraging inefficient and inappropriate training, and favouring larger employers. Those in France and Québec, based upon statutory arrangements rather than voluntary agreement, are perceived as having so few benefits for small employers that they often regard it simply as a tax. Similarly, Australia's experimental Training Guarantee Levy increased substantially private sector spending on training, but was noticeably less effective with regard to small employers.

However, evidence shows that levies can be an effective instrument in relation to small employers. In Spain, they are deployed to encourage firms with fewer than 100 employees to cooperate over training. By requiring sector or territorial groups of such employers to submit joint plans, group training programmes have resulted that benefit from reduced costs through economies of scale. Some bids for funds (e.g. auto-repair shops) are from groups made up of virtually all the enterprises in a sector.

Joint funds for training plans in Italy offer yet another demonstration of how levies can be used to target support to small and micro businesses. Administered by the social partners, funds are earmarked for the preparation of training plans, and then training itself (via the issue of vouchers), in firms with fewer than 15 employees. Belgium's levy, set by collective agreement at 0.25% of payroll, supports a fund that operates according to sector training priorities, but includes a specified minimum to be spent on 'at risk groups', defined to include small businesses.

Rights to training leave

Whether by statutory right for employees or collective agreements, training leave is a direct means of encouraging CVT. While such instruments can be focused upon small businesses, most study leave schemes do not discriminate by firm size, targeting instead disadvantaged employees (e.g. those who are, or are at risk of becoming, unemployed in Sweden, and the less educated in

Denmark). Some countries (such as Spain and South Korea) fund such leave through employer (and employee) contributions to a special training fund. In others (e.g. the Netherlands), leave is funded through special sector training and development funds. By contrast, in Portugal employers are expected to bear the cost of the compulsory training leave (20 hours per year).

Nowhere, however, is take-up of training leave schemes high; less than 2% is typical. The stumbling block, especially for small employers, is how the leave costs – training fees, wages of the absent employee, and costs of replacement staff – are to be met. Scandinavian countries achieve somewhat higher rates of leave take-up among smaller firms, not because of targeting by firm size, but because of their more generous financial support overall, plus institutions and social norms that encourage employers to grant such leave. Otherwise, France is notable for its integrated system granting a general right to training with special provision for small firms to receive support to replace a worker on approved training leave.

Job-rotation schemes

Job-rotation potentially offers a solution to the problem of worker absence for purposes of training. Originating in Denmark, such schemes now operate in a several countries. Job-rotation supports CVT through addressing the need to replace an absent worker and to meet the cost of a replacement. Such schemes are often seen as having the virtue of both meeting the training needs of firms and aiding unemployed persons.

Experience shows, however, that such schemes are not necessarily helpful to small firms – in Denmark, for example, they are found to be relevant mainly to larger SMEs. However, similar projects in Germany have been designed so as to play a significant role with respect to smaller enterprises, including micro-firms. Some localities have developed a substantial support infrastructure purposely orientated to the needs of small firms in particular sectors, where replacement workers are carefully prepared in advance of taking up a position. The scheme is used mostly for replacement of skilled workers and managers rather than the unskilled; thus, not all unemployed people are suitable for such programmes.

Networks and resource pooling

Pooling of resources is commonly used to address various obstacles to training confronting individual small firms. It may involve local or sectoral cooperation among SMEs themselves, or between larger firms and their supply chain partners, including small firms. Evidence from overseas suggests that developing networks can not only strengthen engagement of small firms in training, but also give rise to further benefits based on opportunities for knowledge exchange. The use of collective funds (e.g. from levies) is one example of pooling resources – as in Spain (mentioned above), where small firms submit joint bids for levy funding to cover costs of common training programmes.

Austrian automobile manufacturer Magna Steyr organises training for its supplier network, partly motivated to do so because of quality and other production gains. SME engagement is encouraged by prospects of access to the supply chain, on achieving the requisite accreditations. Belgium's Strategic Plan Kempen (European PLATO programme) funds large enterprises to provide an intensive counselling programme for owner-managers of small local firms. Managers act as mentors, providing individual coaching alongside structured seminar programmes and activities. Evaluation found sustained benefits in terms of both business performance and network building.

In South Korea, companies like Sanyo, aided by payroll tax monies, operate joint training centres for their suppliers, including small firms. Alongside these networks, training consortia of SMEs appoint training managers to liaise with local providers to deliver members' training needs. Evaluation shows that the approach results in training that is more relevant, of improved quality, and available at lower cost. Ireland's enterprise-led Skillnets programme is another successful variant on this model, with 55 sector or area-based networks in operation – all focused upon small firms.

Joint action by business associations, colleges and groups of enterprises is facilitated by programmes such as Canada's Workplace Skills Initiative. WSI funds partnerships to explore innovative ideas for building SME workplace skills through forming new local or sectoral networks of training providers and enterprises, including larger firms.

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4. Conclusion and policy implications

Relevance of overseas experience to the UK

The Leitch Review, National Skills Forum and the UK Commission's skills strategy (2009) stress the importance of employer engagement to the development of skills in the UK, and within this the need to give attention to small firms. This edition of Praxis has discussed the obstacles to small employer engagement in training, and the different approaches taken in other countries to overcome market failures and other obstacles that restrict training efforts in such firms, especially with respect to more formal types of training.

In assessing the relevance to the UK situation of intervention mechanisms successfully deployed overseas, it is important to keep in mind that institutional and cultural factors condition the way that individual policy mechanisms impact upon the decisions of small employers. It should also be recognised that the impact of individual measures are influenced by the broader policy framework within which such interventions operate, and the way in which different aspects of intervention combine to influence the behaviour of key actors.

1. To develop demand-led training in the UK, policymakers should consider going beyond demonstrations of the 'bottom line' value of training, based on achieving an efficient investment level in a static sense. **There is considerable potential in approaching the issue from a dynamic perspective**, i.e. encouraging skill enhancement as a logical and necessary dimension of innovation and product/service quality enhancement, such as constituting an element of a high performance working approach.

In Scandinavia, especially, strategies commonly seek to raise productivity and competitiveness through organisational development, within which skills investment is integral. Such initiatives are widely found to be relevant to small firms. Differences between the UK and Scandinavia – relating to the level of state investment in training and workplace institutions – should not rule out the application of initiatives in the UK to encourage workplace development and more ambitious production objectives. However, it is higher technology firms that tend to engage most readily with the concepts involved, and a key challenge is how to extend the interest in such approaches among firms with less skilled workers and more routine processes.

2. The **need to improve the flow of information to firms is widely recognised**, and experience overseas suggests that England's Train to Gain system – giving special attention to 'harder-to-reach' firms, including small employers – is an effective model. In particular, operating through Business Link helps business brokers to link their work on skills with broader aspects of business strategy. Similar observations might be made of HR Development Advisors in Wales, working through 'Flexible Support for Business'.

3. **Tax incentives should not be regarded as a prime mechanism for encouraging training among small employers**. Relatively high incentives appear to be required, bringing the risk of substantial deadweight costs. Any attempts to incentivise small firms via tax deductions should consider targeting support on additional training by such employers, guided by experience of such schemes applied overseas.

4. The use of direct employer subsidies varies as between the different parts of the UK, with Scotland and Northern Ireland focusing more upon particular groups, compared to Wales and England. Overseas evidence suggests that, appropriately targeted upon small firms, **direct subsidies have the potential to positively affect training**. However, the design of such schemes needs to take account of the issues of administration costs and deadweight. Moreover, experience suggests that subsidies may be most effective when deployed supportively as part of other interventions, such as networks or training leave.

5. To the extent that fear of poaching may restrict a small firm's investment in training, **payback contracts are a potentially useful tool**. However, such devices do not appear to be used in this targeted way and are not without their practical problems (e.g. enforcement, discouraging employees from taking training). Moreover, training itself is thought to reduce losses of staff to poaching through engendering staff loyalty.

6. **Leitch, the National Skills Forum and the UK Commission's Collective Measures Report** where they are appropriate to the sector's labour market conditions and the majority of firms are supportive. Appropriately designed, levy funds administered through collective or sector bodies can positively influence the level and type of training undertaken by small enterprises (as well as promoting training of less qualified workers).

7. **Statutory rights to training leave convey an appropriate message**, but depend for success upon resources available in support. England favours the less directive 'Skills Pledge' – whereby employers, supported by government funding, agree to support eligible employees to gain basic skills and a level 2 qualification; Wales has its own equivalent to this. A statutory entitlement to workplace training is mooted by Leitch, should the Pledge prove to be insufficiently effective and the Collective Measures study suggested piloting supported employer networks to help inform this decision.

This would chime with practice in many countries, where experience supports Leitch's view that financial support may be needed for small employers, to help cover both the absent employee's wages and costs of replacement staff.

8. While **UK experience with job-rotation schemes has been somewhat mixed**, they do address the main problem with releasing staff – the difficulty of providing cover. Experience overseas suggests that job-rotation is potentially of considerable value in helping even the smallest firms to train their workers, especially in some sectors and localities. However, it is far from a cheap policy option, and – from an active labour market policy perspective – is unlikely to benefit significantly the low skilled unemployed.

9. Collaboration among firms – including vertically between large firms and their suppliers – can effectively address market failures restricting training by individual firms acting alone. There is a wide range of network formulations whereby resources can be pooled. Such **networks can both strengthen small employer engagement in training and give rise to other benefits based on associated networking and knowledge exchange**.
While successful examples exist of UK consortia (e.g. in aerospace and automobiles) that support member firms, including through training of SME suppliers, evidence suggests that networks may need support to develop, and there exist overseas examples of initiatives designed for this purpose.

The various examples of international practice outlined here reveal a number of policy options that could help the UK to improve the training rate of its small businesses and ultimately its overall skills profile. These options for small firms need to be assessed in light of the UK context: its voluntarist tradition; existing training and business support infrastructure; and of course the financial context in which future policy must be implemented but highlight ways in which targeted intervention may be used to encourage small firms to invest in training.

5. Recommended readings

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Notes

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