



FICIL
RAISE THE BAR!



Position Paper No. 5

Foreign Investors' Council in Latvia Position Paper on Higher Education and Requalification

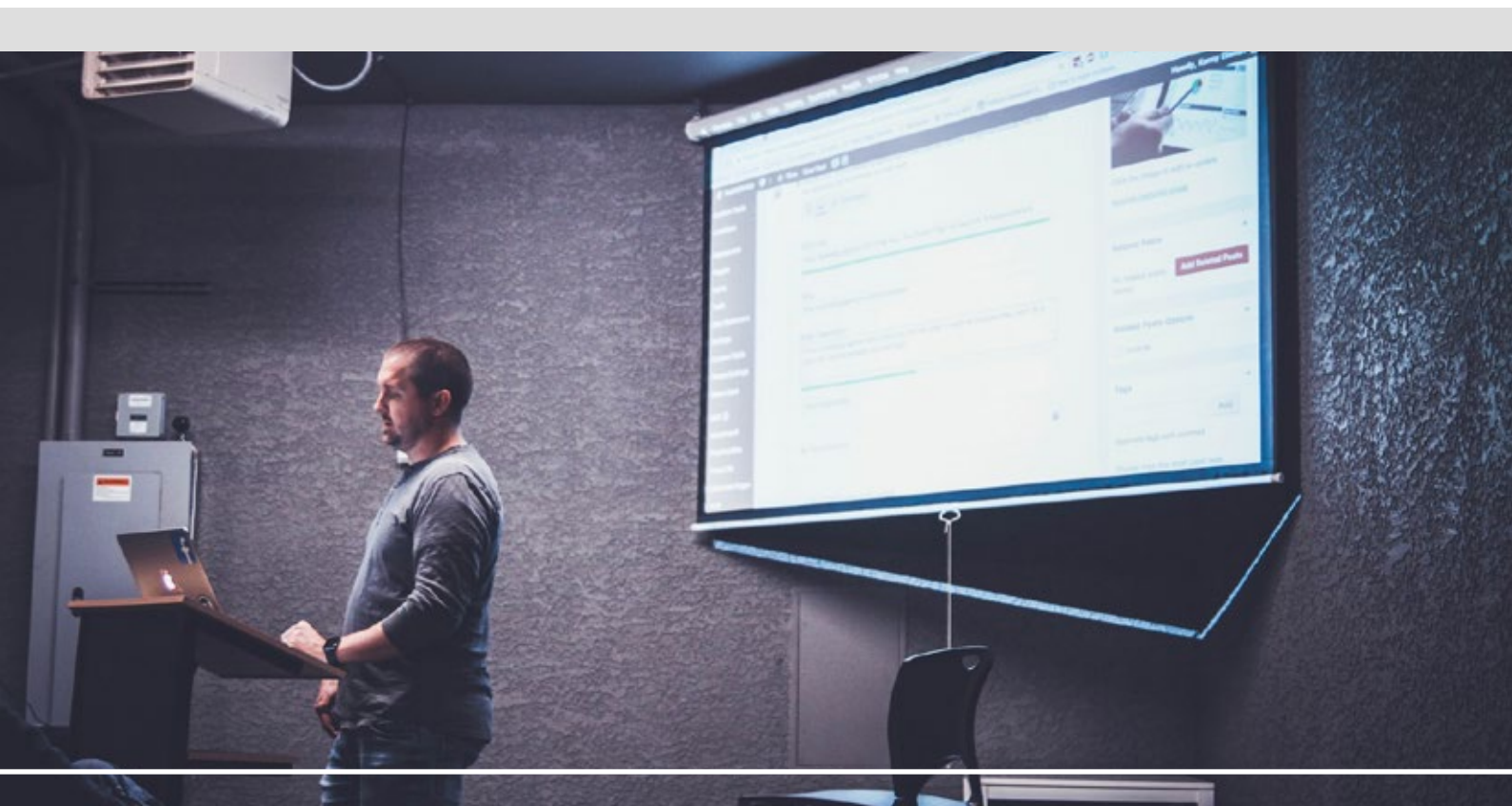
16 September 2021



Executive Summary

The Foreign Investors' Council in Latvia (hereinafter - FICIL) believes that the labour force policy is one of the key drivers of Latvia's economic development. Recognising that education plays a vital role in ensuring that the workforce is equipped with the skills necessary for the modern market, FICIL welcomes the higher education reform and sees it as an important precondition to increasing the competitiveness of the Latvian education system and universities. At the same time, adoption of the reform by the Saeima in June 2021 was only the first step of the reform and its success depends on its implementation. In this Position Paper, FICIL puts forward its recommendations regarding the implementation phase, focusing on the capacity of the Ministry of Education and Science, consolidation of higher education institutions, best practice application and funding.

In the age of rapid digitalisation and robotisation, lifelong learning and continued improvement of skills are an integral component of economic activity, benefiting both employees and employers in promoting the competitiveness of both groups. Considering the current circumstances surrounding the pandemic and its effect on the labour market, the government should review its human capital and workforce requalification policies, to ensure that the decision-makers are able to act proactively to benefit from global trends, prevent large scale unemployment and increase the competitiveness of Latvia. At the same time, these policies should also be closely linked to other medium and long-term national planning documents and prioritised industries. Furthermore, the framework for employers to engage in the training and upgrading of the qualifications of employees should be improved to better represent the interests of employers and incentivise them to invest in their employees.



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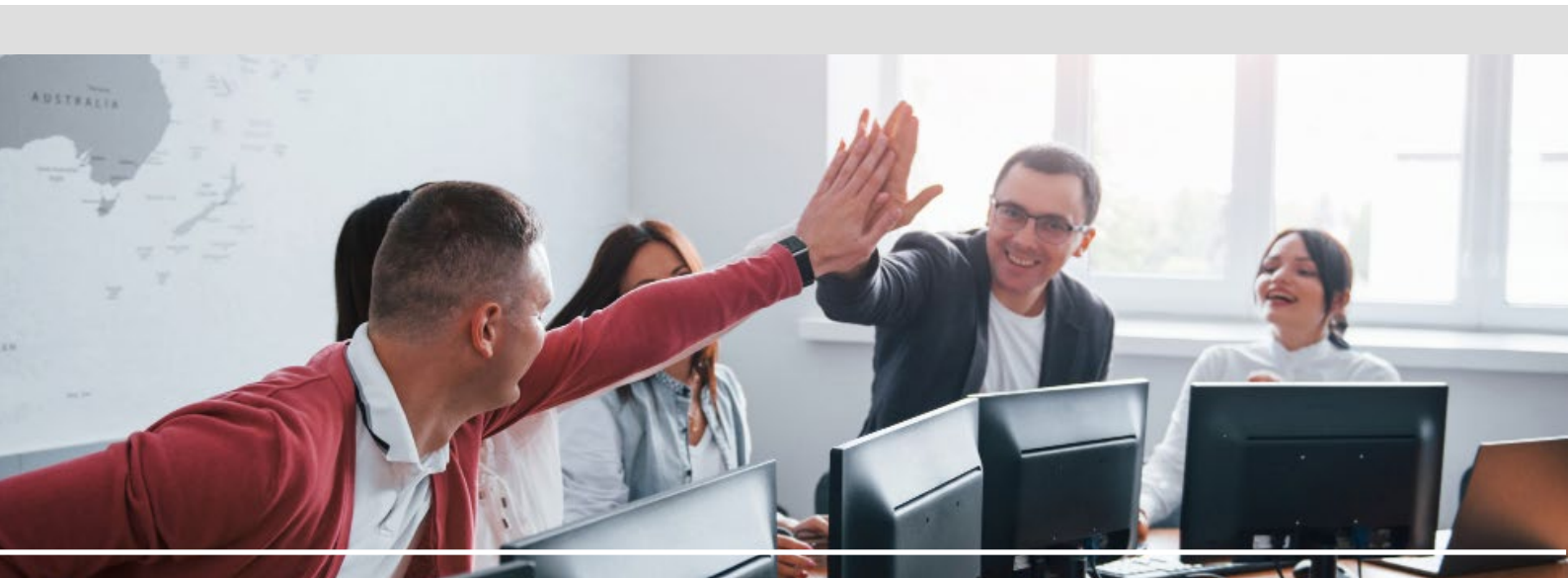


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Recommendations



Higher Education Reform

FICIL welcomes the amendments to the Law on Higher Education Institutions (HEIs) adopted by the Saeima in the third reading on 8 June 2021. The changes introduced in the law, particularly the introduction of external stakeholders in the governance, are a strong development towards increasing competitiveness of our universities.

As FICIL already pointed out in its recommendations in May 2019, a more solid governance system can serve as an important tool in addressing the gaps identified by the State Audit Office and other organisations: a lack of monitoring of the institutions, a lack of efficiency in the management of funding, difficulties for the engagement of talented academic and research experts, available funding per student and the excessive number of institutions¹.

However, adoption in the Saeima is only the first step of an effective reform. The involved parties need to maintain the same enthusiasm in order to achieve the solid implementation of the law amendments.

Therefore, FICIL highlights the following concerns in the implementation and recommends as follows:

1. Strengthen the capacity of the Ministry of Education and Science for the implementation of the reforms.
2. Stimulate the consolidation of the institutions in order to increase their capacity for achieving the fundamental goals of the reforms.
3. Closely monitor and support the steps in the reforms in a selected number of institutions, which could become the model for other HEIs.
4. Review the funding mechanism of the higher education system, considering the objectives of the reforms, the limitations of the current funding system and the exceptional opportunities provided by the Recovery and Resiliency Facility (RRF).

¹ <https://lrvk.gov.lv/lv/revizijas/revizijas/noslegtas-revizijas/vai-augstakas-izglitiba-sistema-ir-efektiva>

Requalification policy

It is a well-known fact that the labour market has been changing rapidly over the last decade and that it will continue this trend also in the foreseeable future. In the current situation, where many new industries are emerging or reshaping, it is vital that Latvia not only retains its international competitiveness, but also uses this opportunity to emerge as a regional leader in terms of a workforce that is equipped with the skills required for the modern job market. Requalification and lifelong learning play a significant role in this, providing the tools for the relatively flexible (compared to formal education) advancement of skills.

Strong and efficient governance of the requalification policy is necessary to make sure that Latvia reduces the ever-increasing skills gap and, therefore, remains an attractive place for investment. For this reason, FICIL recommends as follows:

1. Reform and centralise the governance over the requalification and upskilling policy.
2. Align the requalification and upskilling policy with the long-term government planning documents on economic development.
3. Conduct a proactive skills gap analysis.
4. Review the procedure for the selection of courses that are financed from State and EU funds.
5. Introduce a 'learning pathways' framework.
6. Increase the active engagement of business in the selection, implementation and monitoring of upskilling projects.
7. Revisit the objectives for the requalification in digital skills with clear goals for each segment of the population.

Employers' investments in education and upgrading of qualifications

In FICIL's opinion, the current Labour Law framework does not effectively protect the investments by businesses into upgrading the qualification of employees. The Labour Law does not provide for employer's rights to request the reimbursement of training costs that are related to the change of an employee's position with the same employer (e.g. in case of promotion or change to another position (requalification)). The Labour Law also does not provide the right to enter into agreements on employee training for longer than two years in situations where the employer has invested substantial amounts in the training of the employees.

In order to encourage the investment by employers into the further education of employees and to reconcile the rights of employers and employees, FICIL proposes amendments to Section 96, Paragraph two of the Labour Law, providing that an agreement on training expenses can also be entered into in situations, where the training is related to the change of an employee's position with the same employer. Furthermore, FICIL proposes to amend Section 96 of the Labour Law, providing that, in certain exceptional cases, the term of the agreement on professional training may be three years, particularly, if such training costs exceed 20 minimum monthly salaries as established by the State. At the same time, the Labour Law would retain a provision whereby the amount to be repaid be reduced proportionally to the time the employee worked for the employer after the end of the training.

Meanwhile, if an employer wishes to cover an employee's expenses for obtaining a higher education, these payments will be treated as an employee's income and subject to personal income tax and the corresponding mandatory social security deduction. Considering that the position of the Government of the Republic of Latvia is also to facilitate the acquisition of a higher education where possible and the provision of high value added services, the current regulation of the Law on Personal Income Tax (PIT Law) and Cabinet Regulation No. 899 "Procedures for the Application of the Provisions of the Law On Personal Income Tax" does not actually contribute to the achievement of the aforementioned objectives, but in fact does the exact opposite - prevents employers from investing financial resources in the acquisition of a higher education by employees. Thus, FICIL recommends that Paragraph 18.², Sub-clause 3.1 of Cabinet Regulation No.899 of 21.09.2010 "Procedures for the Application of the Provisions of the Law On Personal Income Tax" be deleted.

Rationale for the recommendations

Higher Education Reform

FICIL strongly believes that changes to the governance model in HEIs is an important pre-condition that will act as a catalyst for further improvements in the education system. The reform will improve transparency and accountability in the governance of HEIs, provide a clear balance between decision-making and executive roles, and enhance the connection with the job market trends. Therefore, we congratulate the Ministry of Education and Science, as well as the Saeima Education, Culture and Science Committee on their persistent work in achieving this milestone on Latvia's way towards becoming an innovation driven society with a strong knowledge ecosystem, based on excellent education and competitive research.

However, adoption in the Saeima is only the first step of an efficient reform. As the success of implementation is largely in the hands of the HEIs, it is important that the corresponding further regulations of the Cabinet of Ministers are developed in close cooperation with them, so that the requirements are realistic and relevant to reach their goal.

Also, it must be recognised that the creation of 17 HEI councils in a relatively short time period is a challenge, given the availability of qualified professionals that could serve as council members. At the same time, it is clear that without strong council members it would not be possible to reach the goal of the councils, as anticipated by the legislator.

This can be resolved through the pooling of resources. Firstly, HEIs could encourage their alumni to apply for the positions of council members. Secondly, the process of final selection should be entrusted to experts in headhunting. Furthermore, at a more strategic level, HEIs should be encouraged to start the process of consolidating their institutions through the creation of joint councils. Notably, this would allow not only the attracting of stronger council member candidates, but also potentially enhance the quality of studies and research through the increase of a critical mass in the institutions.

Requalification policy

The Future of Jobs Report 2020 by the World Economic Forum (WEF) shows that 50% of all employees will require reskilling in the next five years². Even if an employee remains in their current role, it is estimated

that around 40% of the core skills required for their role will change over the same five-year period. The WEF report also highlights the role of the government in providing the opportunities for employees to be able to adapt to the changing market needs. Furthermore, WEF explicitly calls for countries to provide stronger support for reskilling and upskilling for at-risk or displaced workers.

For this reason, it is crucial that the offer for requalification is effective, sufficient and adequate. At the same time, there must be a long-term vision in policy-making, consistency in the determination of priority sectors and clear responsibility over the achievable results. Currently, however, there seems to be no link between the country's plans for economic development and its requalification policy.

Although there are some overlaps in the priority sectors among the State Education Development Agency (VIAA), Investment and Development Agency of Latvia (LIAA) and the National Industrial Policy Guidelines for 2021-2027 (NIPP2027), there are also significant differences. For example, the industry expert councils that shape VIAA's course offer do not reflect some of LIAA's priority sectors, such as healthcare and food manufacturing. At the same time, there is also no clear link to two of NIPP2027 priority directions - bioeconomy and smart materials. As Latvia has defined its future goals in certain economic sectors, it should also be assessed how to ensure that the necessary professionals are available in these fields.

The misalignment of priorities arises due to a lack of centralised policy-making and a lack of decisions based on data. This fragmentation is also causing a lack of clearly defined responsibility in the public sector, as the fact that there are many ministries and agencies involved with the requalification policy results in a situation where there are no common KPIs, harmonised action plans or accountability over the end result. A centralised governance model would be more efficient in responding to the labour market needs. FICIL sees that an expansion of the State Employment Agency's (NVA) mandate could be one potential way to approach this problem. **Annex 1** provides a more detailed overview on how NVA could serve as the central policy-implementer in the area of human capital.

² http://www3.weforum.org/docs/WEF_Future_of_Jobs_2020.pdf

Furthermore, a review of the course content that is made available from the public funds would help to make sure that the offered training corresponds to the country's economic development ambitions and the expected digitalisation of the economy. For example, the ICT sector demonstrates that a formal higher education is unable to produce enough specialists and the industry is lacking over 2000 additional ICT graduates per year³. High-quality upskilling courses can help to narrow this gap. Such high-quality courses require strong collaboration with the industry to identify the specific missing skills, design the course offer and attract qualified trainers.

Finally, there is a need to revisit the objectives that Latvia has set for the upskilling in digital skills. Latvia's plan for the utilisation of the Recovery and Resilience Facility (RRF) includes investments into improving the population's basic digital skills with the goal of increasing the proportion of people with such skills from 43% to 70% until 2027. However, as was evident in the Saeima Education, Culture and Science Committee discussions, various stakeholders in the public sector have very different perceptions on what should be considered as "basic digital skills". Secondly, there are multiple ministries that are planning to be involved in this advancement of skills, however, the RRF plan does not show specific KPIs for each ministry. As a result, such a fragmented approach is likely to lead to overlapping actions and unclear responsibility.

³ http://certusdomnica.lv/wp-content/uploads/2017/10/web_CertusZinojums_2017_1dala_Latvija2022-2.pdf

Employers' investments in education and upgrading of qualifications

Section 96, Paragraph two of the Labour Law currently prescribes that an agreement regarding the reimbursement of costs for the upgrading of qualifications of an employee may only be entered into where the measures for upgrading qualifications are related to the work performed by the employee, but are not crucial for the performance of contracted work. Thus, under the current framework, a situation arises in which the employer is not entitled to recover the costs of upgrading the qualifications of the employee, the need for which is determined by the nature of the specific job.

In FICIL's opinion, the limit prescribed by Section 96, Paragraph two of the Labour Law has no legal grounds. On the contrary, this unnecessarily prevents employees from obtaining the necessary job qualifications. In fact, in this situation, it is the employees that suffer as employers do not wish to risk and pay for this type of training with no guarantee that it will be possible to recover the costs if the employee resigns. If employers cannot retrain existing employees in Latvia, they are forced to search for a workforce abroad, or at least partially transfer their economic activities abroad. Such approach is also supported in other EU / EEA countries, however, may raise substantial concerns in the future related to the training of employees and should be addressed.



Section 96, Paragraph two of the Labour Law sets out additional criteria to be met to allow an agreement between an employer and employee regarding training. One such criteria fundamentally protects the interests of employees by providing that the training expenditure to be reimbursed is reduced proportionally according to the time the employee worked for the employer following the end of the training. FICIL considers that such mechanism protecting employees' rights in the Labour Law should be maintained.

In FICIL's opinion the solution whereby an employer may request the reimbursement of those costs incurred for upgrading the qualification necessary for the performance of the relevant work, in case of a change in an employee's position with the same employer, would partially reconcile the rights of employers and employees. In addition, the maximum period for such an agreement within which the employer is entitled to recover at least part of his investment should be extended to three years if such training costs exceed 20 minimum monthly salaries as established by the State.

Therefore, in order to ensure the opportunity of implementing the reimbursement of training costs, as well as to encourage employers to invest in further training and to reconcile the rights of employers and employees, FICIL proposes that the following amendments be made to Section 96, Paragraphs two and four of the Labour Law:

[..]
(2) *If vocational training or measures for upgrading qualifications are regarded as such which, according to the circumstances, are related to the work to be performed by the employee, yet such occupational training or further education (for the purpose of enhancing the employee's competitiveness) does not have a decisive importance for the performance of the contracted work, or work related to a change of the employee's position with the same employer, the employer and the employee may enter into a separate agreement on the employee's vocational training or upgrading of qualifications and covering the related expenses (hereinafter - the agreement on training).*

(4) *The agreement on training of an employer and employee shall be permissible only where the agreement in question conforms with the following:*

[..]
2) *the term of agreement does not exceed two years or three years if training costs exceed 20 minimum monthly salaries as established by the State starting from the issuance date of an education document certifying the occupational training or upgrading of qualifications;*

[..]

The current provision of the PIT Law deters employers from become engaged in the education of employees, by covering the costs of acquiring a higher education. That is, Section 8, Paragraph two of the PIT Law provides that *"salary, bonuses, one-off and systematic remuneration and other income received by the employee on the basis of current or previous employment relations in commercial companies (...) shall be added to the income for which the salary tax has to be paid in accordance with Cabinet Regulations"*. In turn, Paragraph 18.², Sub-clause 3.1 of Cabinet Regulation No.899 of 21.09.2010 "Procedures for the Application of the Provisions of the Law On Personal Income Tax" determines that: *"for the purposes of applying Section 8, Paragraph two of the Law, income for which no salary tax has to be paid is the expenditure covered by the employer for the training of an employee in order to acquire, improve or extend the skills and knowledge necessary for work, occupation, position or trade (except for the acquisition of a general education and the acquisition of a higher education)"*.

Thus, if an employer wishes to cover an employee's expenses for acquiring a higher education, these payments will be treated as an employee's income and subject to personal income tax and the corresponding mandatory social security deductions.

Considering that the position of the Government of the Republic of Latvia is also to facilitate the acquisition of a higher education where possible and the provision of high value added services, the current regulation of the PIT Law and Cabinet Regulation No 899 "Procedures for the Application of the Provisions of the Law On Personal Income Tax" does not actually contribute to the achievement of the aforementioned objectives, but in fact does the exact opposite - deters employers from investing financial resources in the acquisition of a higher education by employees. Thus, FICIL recommends that Paragraph 18.2, Sub-clause 3.1 of Cabinet Regulation No.899 of 21.09.2010 "Procedures for the Application of the Provisions of the Law On Personal Income Tax" be removed.

Annex 1 - State Employment Agency as a central platform for human capital management

Human capital is one of the key drivers of Latvia's economy, therefore, labour force policy is paramount to shaping Latvia as an attractive place for investment. Fragmented policy-making and implementation process lead to slow decisions, unclear priorities and a lack of governance over the required actions and expected results. It is essential to centralise decision-making and implementation process in this policy field, in order to make sure that Latvia is able to respond and proactively react to the rapidly changing labour market needs.

FICIL has identified the State Employment Agency (NVA) as a potential central figure in the implementation of labour force policy. At the moment, NVA is primarily an agency that works with the unemployed under the Ministry of Welfare. Nevertheless, FICIL sees that NVA could be transformed into an overarching policy-implementer responsible for the entire labour force. This would also include centralised governance over the requalification policy which is imperative to ensuring the availability of skilled labour over the coming years.

Such developments would require extending NVA's current mandate and strengthening its capacity to conduct in-depth analysis, including data analysis. By redesigning NVA into a centralised platform for the compilation of opinions, research and analysis in the field of labour policy, Latvia would have a competence centre that can take appropriate strategic actions based on a thorough skills gap analysis and timely identification of required skills. Consequently, the education offer can then be reprofiled to match the labour market needs and long-term national and international trends.

Improving the approach towards human capital issues would allow the positioning of Latvia in the eyes of foreign investors as a country with a stable, considered

and data-based labour force policy. Long-term success that is based on data and research requires that the topic of human capital development in Latvia receives the highest political priority and is supported accordingly.

Setting NVA as the key player and centralising the policy implementation would also lead to efficiency gains in the upskilling course offer. It is evident that in terms of requalification and lifelong learning, the functions of NVA and the State Education Development Agency (VIAA) overlap. Both agencies offer courses for requalification with almost identical course and trainer selection criteria. FICIL strongly believes that State financed courses should serve the purpose of providing quality upskilling opportunities for people looking to upgrade their knowledge and skills to further apply them in the job market. Therefore, this proposal could lead to better employee profiling, improved governance over the course offer, clear targets and accountability over these targets.

Examples from other countries include the Danish Agency for Labour Market and Recruitment (STAR)⁴. STAR is responsible for implementing and monitoring the labour policy in Denmark, while also closely collaborating with the relevant ministry in policy formulation and drafting of legislation. Furthermore, STAR serves as a centralised knowledge hub that supports other ministries, the parliament and other policy-makers. STAR is specifically focused on addressing the opportunities and challenges of the future job market.

⁴ <https://star.dk/en/about-the-danish-agency-for-labour-market-and-recruitment/>



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FICIL is a non-governmental organisation that unites 38 largest foreign capital companies from various industries, 10 foreign chambers of commerce in Latvia, French Foreign Trade Advisers and Stockholm School of Economics in Riga. The goal of FICIL is to improve Latvia's business environment and overall competitiveness in attracting foreign investment, using the experience and knowledge of its members to provide recommendations to Government and state institutions.

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