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## Direction and Challenges of Establishing Subsidiaries of the Public Institutions\*

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Soonwon Kwon, Kyetaik Oh\*\*

### I. Introduction

During the past several months since the launch of the Moon Jae-in government, a number of public institutions, the central government and local governments have been following necessary procedures to convert non-regular workers into regular workers in an effort to carry out one of the government's key policy tasks. Although some public institutions have faced delays or even discontinuation of the conversion process due to certain controversial issues and obstacles, most of them have actively implemented the project to grant regular status to non-regular workers. Based on the cases observed so far, the types of hiring available in the course of regularizing non-regular

jobs in the public sector are: direct hiring, hiring through subsidiaries, and setting up other types of corporations (foundation or cooperative). Direct hiring would be the best option given the purposes and objectives of the government's policy, but differing situations (for example, the size of personnel subject to conversion is big; the types of jobs subject to conversion are significantly different from the core jobs within institutions; or other unique circumstances of institutions) could inevitably require hiring through subsidiaries.

However, the labor community has been opposed to hiring through subsidiaries because of the problems in the governance and management of subsidiaries observed so far. Most noticeably, the wage and welfare gaps be-

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tween parent institutions and their subsidiaries are serious because there have been many cases in which the subsidiaries in the public sector were used simply as a contract firm supplying labor or as a means to increase cost efficiency. In addition, some are opposed to hiring through subsidiaries because of the unstable employment status of workers of the subsidiaries, and there is also concern about possible outsourcing of their jobs to the private sector in case of emergency.

There are several ways to respond to such real needs and concerns: to permit hiring through subsidiaries only for inevitable circumstances, to maintain the independence and operational rationality of governance when establishing subsidiaries, and above all, to encourage subsidiaries to rationally design and operate their workers' employment status, wages and working conditions. On the assumption that hiring through subsidiaries is inevitable for various reasons, this paper explores the legal basis for the establishment of subsidiaries, how to set up contracts, and how to maintain the independence of governance and management. Furthermore, it examines ways to prevent the gap between workers of parent companies and those of subsidiaries in terms of employment, wages and working conditions.

## II. Subsidiary: Definition and Status

### 1. Definition of a Subsidiary

According to the Commercial Act, a subsidiary company is defined as one of which more than half of the total number of issued and outstanding shares is owned by the parent company. In the public sector, a subsidiary company refers to a company established by investments or

funds provided by public institutions (public corporations, quasi-governmental institutions) or local public enterprises. With regard to this, an instruction of the Ministry of Economy and Finance <sup>11</sup> (The Regulations on Contracting Affairs of Government-Owned Corporations and Quasi-Governmental Institutions, The Ministry of Economy and Finance Instruction No. 571, Sep. 12, 2016) defines a subsidiary company as “a juristic person in which the relevant public corporation or quasi-governmental institution holds at least 50/100 of the total number of issued stocks or total shares of investment.” On the other hand, according to the regulations regarding in the Enforcement Decree of the Local Public Enterprises Act, a subsidiary company refers to “a juristic person in which the relevant corporation holds 100/100 of the total number of issued stocks or total shares of investment.”

In short, a public institution establishes a subsidiary company by providing investments of 100% (local public enterprises) or over 50% (public corporations and quasi-governmental institutions) to entrust or delegate its affairs. Thus, in terms of the percentage of shares, local public enterprises exercise stronger ownership and domination over their subsidiaries than public corporations and quasi-governmental institutions do.

#### The Regulations on Contracting Affairs of Government-Owned Corporations and Quasi-Governmental Institutions

Article 8 (Negotiated Contracts) (1) The head of the government-owned corporation or quasi-governmental Institution or a contracting officer may conclude a negotiated contract in any of the following cases:

1. Where he/she intends to conclude a contract with the central government or a local government;

11) Upon entrustment by Article 39 (3) of the Act on the Management of Public Institutions, this instruction prescribes necessary matters concerning the standards and procedures for contracting with public corporations and quasi-governmental institutions and restrictions on the qualification for bidding.

2. Where a government-owned corporation or a quasi-governmental institution intends to conclude a contract falling under any of the following clauses with its subsidiary (referring a juristic person in which the relevant public corporation or quasi-governmental institution holds at least 50/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in this Article) or with a company in which it has invested (referring to a juristic person, the total of the number of stocks or shares of investment of which held by the relevant public corporation or quasi-governmental institution and other public corporations, quasi-governmental institutions, or Korea Development Bank is at least 50/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in this Article)

#### Enforcement Decree of the Local Public Enterprises Act

Article 57-4 (Accounting, etc.) (2) Notwithstanding Article 25 (1) of the Enforcement Decree of the Act on Contracts to Which a Local Government Is a Party which applies mutatis mutandis under paragraph (1), the president of a corporation or an employee who takes charge of the affairs related to contracting upon delegation or entrustment of all or part thereof by the president of a corporation (hereinafter referred to as “contracting officer”) may conclude a contract by free contract in any of the following cases

1. Where he/she intends to conclude a contract with a subsidiary of the corporation (referring to a juristic person in which the relevant corporation holds 100/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in subparagraph 2) or a company in which it has invested (referring to a juristic person, the total of the

number of stocks or shares of investment of which held by the relevant corporation and other corporations is 100/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in subparagraph 2) to entrust or delegate the affairs of the corporation

## **2. Status of Governance and Management at Subsidiaries**

In general, parent companies not only appoint the representatives and executives of subsidiaries, but also influence the changes in the organization, the prescribed number of personnel, and the structure and level of remuneration. In the case of subsidiaries designated as public institutions or quasi-governmental institutions, their governance and business management are relatively independent because they operate in accordance with the guidelines of the Ministry of Economy and Finance and the Ownership Steering Committee. On the other hand, in the case of “non-classified public institutions” or other types of public institutions, it is inevitable that their parent companies intervene in the governance and business management of subsidiaries.

### **1) Governance**

Since most subsidiaries of public institutions are those in which the parent institutions hold 100% of the outstanding shares of, their appointment of executives, their design and distribution of the business, the salaries and working conditions of employees, etc., are also directly determined or greatly influenced by the parent institutions. In particular, if a subsidiary is entrusted with a project by its parent company, the wages and working conditions of the employees of the subsidiary is determined by the unit price of services offered by the parent company. Sometimes,

Table 1. Governance of Subsidiaries of Public Institutions

Corporation Name	Date of Establishment	CEO	Previously Held Post	End of Term
<Subsidiaries of Korea Railroad Corporation>				
Korail Tourism Development	August 11, 2004	Bang, Chang-hoon	Head of Operations, KORAIL West Capital Region Headquarters	December 2017
Korail Networks	September 21, 2004	Park, Yool-geun	Policy Advisor to the Minister of Education, Science, and Technology	March 2018
Korail Logis	December 31, 2003	Park, Ki-hong	Head of Business Operations, Hutchison Korea Terminals	January 2018
Korail Retail	December 2, 2004	Yoo, Je-bok	Technical Expert, Root Partners	March 2018
Korail Tech	December 9, 2004	Ban, Geuk-dong	Director of Electricity, KORAIL Busan Gyeongnam Headquarters	
<Subsidiaries of Korea Electric Power Corporation>				
Korea Hydro & Nuclear Power	April 2, 2001	vacant		
Korea South-East Power	April 2, 2001	Yoo, Hyang-yeol	Director of Overseas Operations, Korea Electric Power Corporation	February 2021
Korea Midland Power	April 2, 2001	vacant		
Korea Western Power	April 2, 2001	Kim, Byung-sook	Head of New Growth Engine Division, Korea Electric Power Corporation	March 2021
Korea Southern Power	April 2, 2001	Shin, Jeong-sik	President of Korea Energy Economics Institute	March 2021
Korea East-West Power Corporation	April 2, 2001	Park, Il-jun	Executive Director, Ministry of Trade, Industry and Energy	February 2021
KEPCO E&C	October 1, 1975	Lee, Bae-soo	Vice President, Korea Engineering & Power Services	February 2021
Korea Plant Service & Engineering	April 1, 1984	vacant		
KEPCO KDN	January 23, 1992	Park, Seong-cheol	Head of New Growth Engine Division, Korea Electric Power Corporation	February 2021

Source : All Public Information In-One (ALIO) system ([www.alio.go.kr](http://www.alio.go.kr)). (As of April 17, 2018)

representatives or executive positions at a subsidiary firm function as post-retirement positions for the retirees of the parent company. Thus, under the current structure, subsidiaries bear full responsibility for business management and operation as well as legal matters even though their parent firms are in actual control. This may lead to a problem of whether parent companies are functioning as “employer” with respect to matters relating to employment and labor-management relations.

## 2) Wage

The most outstanding problem in the existing business management of subsidiaries has to do with the wage and fringe benefits of their workers. Most of the subsidiaries

in the public sector have been established for the purpose of reducing costs, and they are often paid very low wages compared to those working in their parent companies regardless of the employment status of their workers (regular or indefinite-term contract). A case in point is Korea Railroad Corporation. The workers of its subsidiaries earn only 50-60% of the wages paid by the parent company. Even if the workers of the subsidiaries perform similar/same tasks as those at Korea Railroad Corporation, they earn significantly lower wages than the parent-company counterparts. Of course, some gaps are inevitable given the relative value of the jobs, competition in the market, and relevance to the core business of the parent institution. However, it is worrying that the wage level of work-

Table 2. Personnel and Salary Status of Korea Railroad Corporation and its Subsidiaries <sup>2)</sup>

	Regular Workers			
	Average Salary Per Person	Average Entry-level Salary	Number of Full-time Employees	Average Years of Service
Korea Railroad Corporation	67,766	30,204	26,954	19.84
Korail Tourism Development	33,240	21,612	776	6.5
Korail Networks	44,690	26,672	88	9.3
Korail Logis	37,675	23,985	62	6.6
Korail Retail	49,337	30,435	298	13.09
Korail Tech	45,479	24,077	43	7.68
	Indefinite-term Workers			
	Average Salary Per Person	Average Entry-level Salary	Number of Full-time Employees	Average Years of Service
Korea Railroad Corporation				
Korail Tourism Development	27,026		23	3.5
Korail Networks	25,029		831	6.5
Korail Logis			0	
Korail Retail	29,599		14	4.06
Korail Tech			0	

Source : All Public Information In-One (ALIO) system (www.alio.go.kr).

Table 3. Wages of Different Types of Public Institutions

	2012	2013	2014	2015	2016
ALL	62,372	63,102	63,592	64,932	66,073
Public Corporations	72,565	72,987	72,224	75,359	79,050
Market-type Public Corporations	76,402	76,447	75,551	77,418	82,195
Quasi-market-type Public Corporations	70,007	70,681	70,006	73,987	76,953
Quasi-governmental Institutions	61,128	62,708	62,615	64,597	65,332
Fund-management-type quasi-governmental institutions	69,011	70,174	70,180	73,179	75,135
Commissioned-service-type quasi-governmental institutions	59,300	61,026	60,979	62,791	63,295
Non-classified Public Institutions	61,129	61,617	62,592	63,420	64,368

Source : All Public Information In-One (ALIO) system (www.alio.go.kr).

ers of subsidiaries is very low irrespective of the services they supply when the subsidiaries exist mainly for the purpose of cost reduction.

On the other hand, in the case of certain firms that are classified as subsidiaries in terms of corporate governance

but engaged in an independent business that is distinct from the business of the parent companies, their employees enjoy remuneration and general working conditions comparable to – or sometimes even better than – those of the parent companies. In short, based on the cases so far,

2) In the case of Korea Railroad Corporation and its subsidiaries, the wage gap may exist depending on the nature of work, the average years of service of employees, and so on. Therefore, it is not desirable to directly compare their wage levels based solely on publicly disclosed data. However, when compared to other institutions of the same type, it is analyzed that both Korea Railroad Corporation (the market-type public corporation) and its subsidiaries (non-classified public institutions) pay lower wages than the average wage paid by other institutions of the same type. In fact, some subsidiaries of Korea Railroad Corporation pay only half of the average wage.

it can be concluded that the wage and working conditions at subsidiaries become a cause for concern only when parent and subsidiary institutions are in subcontract transactions in order to entrust or be entrusted with providing services.

### 3) Employment

Unlike in the case of contracting-out, most of those employed in subsidiaries have either permanent or indefinite-term employment status. As for private partner companies, they hire workers on fixed-term employment contract but take advantage of the exemption from having a fixed employment period (satisfying the ground that 'the period required to complete a project or particular task is specified') under the Act on the Protection, etc. of Fixed-term and Part-time Workers, so their workers continue to

face employment instability whenever their employment contract needs to be renewed upon expiration of services. Therefore, it would be fair to say that the employment status of the employees of subsidiaries in the public sector may be relatively safer. However, there still exist a few fundamental instability factors such as cost pressures resulting from management evaluations, the threat of business restructuring due to changes in policy and market environment, and the streamlining of labor processes enabled by technological developments and the application of intelligent information technology.

Some institutions have more indefinite-term workers than regular employees. In most cases, such circumstances are the result of the choice of those institutions to cover their personnel expenses for indefinite-term workers with their business expenses either because they have a limit-

Table 4. Personnel Status of Korail Networks Co., Ltd.

			2012	2013	2014	2015	2016	2017
Regular	Prescribed Number of Personnel		1,321	1,321	138	138	111	126
	Current Number of Personnel	Total	853	894	104	95	88	105
		Full-time	853	894	104	95	88	105
		Part-time	0	0	0	0	0	0
Indefinite-term	Prescribed Number of Personnel		0	0	1,183	1,183	1,171	1,493
	Current Number of Personnel	Total	0	0	842	778	831	1,081
		Full-time	0	0	842	775	828	1,069
		Part-time	0	0	0	2.5	2.5	11.85

Source : All Public Information In-One (ALIO) system ([www.alio.go.kr](http://www.alio.go.kr)).

Table 5. Personnel Status of KEPCO KDN

			2012	2013	2014	2015	2016	2017
Regular	Prescribed Number of Personnel (B)		1,293	1,293	1,293	1,346	1,466	1,517
	Current Number of Personnel	Total	1,220	1,222	1,236	1,274	1,325	1,417
		Full-time	1,217	1,219	1,233	1,271	1,322	1,415
		Part-time	3	3	2.5	3	2.5	1.5
Indefinite-term	Prescribed Number of Personnel (C)		0	549	549	917	906	949
	Current Number of Personnel	Total	474	515	542	725	702	686
		Full-time	474	515	542	725	702	686
		Part-time	0	0	0	0	0	0

Source : All Public Information In-One (ALIO) system ([www.alio.go.kr](http://www.alio.go.kr)).

ed personnel budget or because they are understaffed for the volume of business being handled. Of course, there are many cases in which subsidiaries in the public sector hire fixed-term workers, temporary agency workers or workers provided by contract firms. That is also a way to circumvent the rules in the budgetary guidelines that limit personnel expenses.

#### 4) Cost Management

Generally, when contracting-out, 20% of the expenses included in the unit cost of services are inevitable expenses – overhead expenses of about 5%, profits for the contract firm of about 5%, and value-added tax of 10%. It is judged that subsidiaries of public institutions would have a similar cost structure. The unit cost of services may increase if certain equipment or facility needs to be procured, but even so, the profit margin is unlikely to exceed 5%.

Except for few that offer exclusive and independent services based on highly specialized expertise and technology, most subsidiaries in the public sector – and private contract firms – are in a subordinate contract relationship with their parent institutions, providing simple ancillary services for them. Since the two are engaged in subcontract transactions in order to entrust or be entrusted with providing simple labor, the wage of the workers of subsidiaries is set at the minimum wage level, and the unit cost of services is determined based on such wage. In a nutshell, in most cases, the cost of services for subsidiaries in the public sector engaged in subcontract transactions is linked to the minimum wage.

In addition, since most of the subsidiaries of public institutions are designated as non-classified public institutions, they are subject to the government's budgetary guidelines, and there are strict restrictions in applying the cost adjustments to improve the working conditions of their workers.

#### 5) Labor Processes

Oftentimes, employees of subsidiaries consider themselves, or are considered by others as “second-class” workers even though they are employees of public institutions. In particular, when parent and subsidiary institutions are in subcontract transactions in order to entrust or be entrusted with providing services, colonial mentality is prevalent among the workers of subsidiaries. Furthermore, when the workers of subsidiaries perform similar/same tasks as those of parent institutions, the former tends to feel different and marginalized, and there is room for illegal dispatch if certain labor processes are mixed.

Even if the physical working space and the system of supervision and command are separated, the service systems are likely to be linked with one another due to the characteristics of public institutions, so it is difficult to set the actual boundaries and divide the tasks. For this reason, in the services of public institutions, the employees of parent companies are likely to be promoted to the position of supervisor, and those of subsidiaries are likely to stay as field workers as a result of organizational integration.

In some institutions, the employees of subsidiaries have been increasingly voicing complaints about the difference in the wages and working conditions that they face even though they provide similar/same labor as the workers of parent institutions.

### III. Establishing a Subsidiary : Requirements and Direction

#### 1. Institutional Requirements for Establishing a Subsidiary

When a public institution decides to establish a subsidiary, the sustainability of the business contract must be guaranteed for the purpose of ensuring stable employment and wage conditions for the workers of the subsidiary. To that end, a negotiated contract between the public



institution and the subsidiary should be recognized. There are two prerequisites to set up a negotiated contract under the current institutional conditions. The first is to add “the government’s employment policy” as a reason for using a negotiated contract in accordance with the ‘Regulations on Contracting Affairs of Government-Owned Corporations and Quasi-Governmental Institutions’; and secondly, to use the approval authority of the Minister of Economy and Finance. However, since the latter is only a temporary solution, it is safe to add a reason for using a negotiated contract within the Regulations on Contracting Affairs of Government-Owned Corporations and Quasi-Governmental Institutions.

Concerning the reasons for using a negotiated contract, Article 39 (3) of the Act on the Management of Public Institutions stipulates that necessary matters concerning the accounting principles and restrictions on the qualification for bidding shall be prescribed by Ordinance of the Ministry of Economy and Finance, and accordingly, the ‘Regulations on Contracting Affairs of Government-Owned Corporations and Quasi-Governmental Institutions’ (hereinafter referred to as “the Regulations on Contracting Affairs”) has been established. Moreover, Article 8 (1) and (2) of the Regulations on Contracting Affairs states the grounds for concluding a negotiated contract between a public institution and its subsidiary as follows:

Article 8 (1), The Regulations on Contracting Affairs of Government-Owned Corporations and Quasi-Governmental Institutions

2. Where a government-owned corporation or a quasi-governmental institution intends to conclude a contract falling under any of the following clauses with its subsidiary (referring a juristic person in which the relevant public corporation or quasi-governmental institution holds at least 50/100 of the total number of issued stocks or total shares of invest-

ment; hereafter the same shall apply in this Article) or with a company in which it has invested (referring to a juristic person, the total of the number of stocks or shares of investment of which held by the relevant public corporation or quasi-governmental institution and other public corporations, quasi-governmental institutions, or Korea Development Bank is at least 50/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in this Article);

- a. Based on the government’s policy to achieve innovation in management, a government-owned corporation or a quasi-governmental institution commissions or delegates some affairs to its subsidiary or a company in which it has invested;
- b. Where it is inevitable to maintain facilities and equipment of the relevant public corporation or quasi-governmental institution, or to maintain Class-I establishments under subparagraph 2 of Article 2 of the Special Act on the Safety Control and Maintenance of Establishments;
- c. Where it is inevitable to protect and nurture specific technology recognized by the head of the competent agency;
- d. Where it is deemed unavoidable by the head of the competent agency to reorganize a subsidiary of a government-owned corporation or a quasi-governmental institution or a company in which it has invested in order to achieve innovation in management of the relevant public corporation or quasi-governmental institution.

Also, Article 57-4 (2) of the Enforcement Decree of the Local Public Enterprises Act states the following regulations on the cases where a public institution may conclude a negotiated contract with its subsidiary as follows:



#### Article 57-4 (2) of the Enforcement Decree of the Local Public Enterprises Act

Notwithstanding Article 25 (1) of the Enforcement Decree of the Act on Contracts to Which a Local Government Is a Party which applies mutatis mutandis under paragraph (1), the president of a corporation or an employee who takes charge of the affairs related to contracting upon delegation or entrustment of all or part thereof by the president of a corporation (hereinafter referred to as "contracting officer") may conclude a contract by free contract in any of the following cases: <Amended on Jan. 28, 2015>

1. Where he/she intends to conclude a contract with a subsidiary of the corporation (referring to a juristic person in which the relevant corporation holds 100/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in subparagraph 2) or a company in which it has invested (referring to a juristic person, the total of the number of stocks or shares of investment of which held by the relevant corporation and other corporations is 100/100 of the total number of issued stocks or total shares of investment; hereafter the same shall apply in subparagraph 2) to entrust or delegate the affairs of the corporation;
2. Where he/she intends to conclude a contract inevitably with a subsidy of the corporation or a company in which it has invested, for the maintenance, etc. of facilities and equipment owned by the relevant corporation or the first-class public structures defined in subparagraph 1 of Article 7 of the Special Act on the Safety Control and Maintenance of Establishment

According to the Regulations on Contracting Affairs, "based on the government's policy to achieve innovation in management, a government-owned corporation or a quasi-governmental institution commissions or delegates

some affairs to its subsidiary or a company in which it has invested" is listed as one of the reasons for concluding a negotiated contract. However, it is not easy to interpret the necessity of negotiated contracts arising from "the government's employment policy," which is the current policy interest, as something linked to "the government's policy to achieve innovation in management." Therefore, in order to consider the case of commissioning or delegating affairs based on "the government's employment policy" or related regulations as a legitimate reason for concluding a negotiated contract, it is necessary to add the reason to each subparagraph of Article 8 (1) of the Regulations on Contracting Affairs.

Another way to set up a negotiated contract without having to add the aforementioned reason to each subparagraph of Article 8 (1) of the Regulations on Contracting Affairs is to utilize the approval system of the Minister of Economy and Finance. According to Article 2 (2) of the same regulations, "the head of the public corporation or quasi-governmental institution (hereinafter referred to as "institution head") may determine the standards and procedures of contracting differently from those stipulated in the Regulations on Contracting Affairs by obtaining approval from the Minister of Economy and Finance when it is necessary to consider the nature of work performed at the relevant public corporation or the quasi-governmental institution, to secure fairness and transparency of the contract, or in extenuating circumstances."

Therefore, if it is desired to conclude a negotiated contract for reasons unspecified in the Regulations on Contracting Affairs, it is possible to do so through the approval of the Minister of Economy and Finance. However, such method should be regarded as a temporary solution, and it is desirable to have a provision related to negotiated contracts expressly stipulated in the Regulations.

Even if these requirements are met, it needs to be examined separately whether negotiated contracts fall under the grounds of illegal assistance under the Fair Trade Act.

However, in this regard, it is difficult to design general rules that encompass all the possible cases as there exist diverse cases with each case having to be dealt or treated as uniquely as possible. Even so, based on the past precedents, when the cost of services is set at an excessively high level under a negotiated contract, the relevant transaction is judged to be an illegal assistance or an unfair transaction. Therefore, it is desirable to stipulate in the law to maintain the cost of services at the market level or to determine the cost at a reasonable level acceptable to society.

## 2. Direction for Establishing a Subsidiary

Based on the analysis of the current status of operating the subsidiaries in the public sector that function as subcontractors, it is difficult not to conclude that ‘it is a form of indirect employment’. Until now, many public institutions have established and operated subsidiaries as a means to avoid their responsibilities and obligations as an employer and to reduce costs. Such reality implies that the wages and working conditions of the employees of subsidiaries are relatively vulnerable.

Therefore, in order not to repeat these past practices, when deciding to hire through a subsidiary as a way of converting the status of non-regular employees to regular workers, it is essential to ensure that the purpose of doing so is not simply to achieve cost efficiency, and that the subsidiary can reinforce its expertise and maintain independence. In addition, it is also important to design the wages, employment and working conditions for the workers of subsidiaries in a practical way, providing balanced treatment for all workers.

Furthermore, if it is inevitable to establish and operate a subsidiary as a subcontractor to entrust it with carrying out a project or providing services, it should be premised on mutual trust and cooperation between the parent institution and the subsidiary, and on an integrated management plan for sharing profits and risks and managing con-

flicts. To this end, institutional reform should take place if necessary. More specifically, it would be desirable to form and operate a parent-subsidiary consultative body, and invite the employer and worker representatives of subsidiaries to participate in the labor-management council of parent institutions.

### 1) Governance

As discussed earlier in the article, most of the subsidiaries in the public sector are companies whose stock is 100% owned by their parent institutions. Due to such circumstances, the parent institutions directly decide or considerably influence such matters as the appointment of executives, the design and distribution of business, the salaries and working conditions of the employees of subsidiaries, and so on. As mentioned above, some subsidiaries are also used as means for outplacement of the executives of the parent institutions. Despite the fact that parent companies are in actual control, they are free from the business and management obligations and legal responsibilities of their subsidiaries.

Therefore, when establishing a subsidiary in the public sector, it is important to clearly set the boundaries of authority and responsibility, exclude the intervention of the parent company in subsidiary management, and design the governance structure to allow independent management of the subsidiary even under limited conditions. It would also be helpful to implement some of President Moon Jae-in’s pledges such as introducing the worker-director scheme or enabling worker representatives to sit on the board of directors.

Above all, establishing subsidiary firms and commissioning business affairs to them should be premised on the prior coordination and consultation of stakeholders within the institutions. Given that commissioning of business affairs to subsidiaries was mainly used as a procedural means for cost reduction and privatization in the past, it is necessary even for subsidiaries in the public sector to

set up proper procedures to address such concerns. Therefore, it may be desirable to introduce the requirement of consulting with labor unions and related stakeholders from the stage of establishing the subsidiaries.

#### (1) The Worker-director Scheme

The introduction of the worker-director scheme not only contributes to realizing economic democracy but also produces the “innovation effect” by applying the field experience and knowledge to business management and the “social effect” by securing the support of employees for controversial management plans through effective communication.<sup>3)</sup> Newly established subsidiaries in the public sector should work on securing management transparency and promoting public interests by facilitating cooperation and mutual prosperity between labor and management through the introduction of a system of participation by workers in the management process,

Considering that, in Europe, stakeholders of public institutions are allowed to participate in the management process because of the purpose of establishing and operating public institutions being linked with public interests and public needs rather than profitability, there seems to be no reason for Korea – where the social role of the public sector is quite big – to hesitate to introduce and utilize such a system. In particular, the worker-director scheme can serve as an effective means of checking the deterioration of wages and working conditions that could result from the division of business into parent institutions and subsidiaries.

#### (2) Parent-Subsidiary Joint Labor-Management Council

The issue of representing the interests of employees of both public institutions and their subsidiaries often goes beyond the workplace level. In particular, while the matters relating to employment, wages and working

conditions of the employees of the subsidiaries are often dependent on the parent companies, the workers of the subsidiaries are excluded from the parent companies’ decision-making process including collective bargaining.

For this reason, it is necessary to consider the establishment and operation of the Parent-Subsidiary Joint Labor-Management Council which can represent the workers belonging to public institutions and their subsidiaries.

Although this method cannot be enforced by the Act on the Promotion of Workers’ Participation and Cooperation, both public institutions and their subsidiaries could consider the purpose of establishing such a body with a forward-looking perspective and agree to set up a joint labor-management council where they can coordinate and negotiate the employment and working conditions of the workers belonging to public institutions and their subsidiaries. Through such a council, both parties can discuss matters including the employment, wages and general working conditions of the employees of subsidiaries, and seek ways to expand collective benefits for both labor and management through the development of integrated agendas for public institutions and their subsidiaries.

### 2) Wages and Working Conditions

#### (1) Narrowing the Gaps among Institutions

As discussed earlier, the biggest problem in the management of subsidiaries is the wage level. Most of the existing subsidiaries in the public sector have been installed for the purpose of cost reduction. Some subsidiaries pay only about 37% of the average wage paid by their parent institution, which is only about 40% of the average wage of non-classified public institutions – the category to which the relevant institutions belong. However, it is realistically difficult to significantly improve the wage level for subsidiaries with particularly poor working conditions under the

3) Park, Tae-ju (2016), *How is it possible to introduce the board-level employee representation in Korea?*, Labor Law Forum Issue No. 19, Society of Labor Law Theory and Profession, p.43.

budget guidelines of the Ministry of Economy and Finance.

Currently, a ‘target-setting method’ is used when eval-

### 2017 Guidelines for Budget Compilation

#### ☐ Personnel expenses

##### (1) Total personnel expenses

☐ The 2017 budget for total personnel expenses shall be compiled by increasing the 2016 budget for total personnel expenses within 3.5%.

- *Provided*, that if the 2015 average wage per person for regular employees (including indefinite-term workers) is not higher than 90% of the industry average and not higher than 60% of the public sector average, the budget increase shall be made within 5.0%; if it is not higher than 90% of the industry average and not higher than 70% of the public sector average, the budget increase shall be made within 4.5%; and if it is not lower than 110% of the industry average and not lower than 120% of the public sector average, the budget increase shall be made within 2.5%.

☐ In principle, the budget for total personnel expenses will be compiled based on the prescribed number of personnel (including indefinite-term workers) as of the end of 2016, but the personnel expenses for existing personnel and indefinite-term workers shall be managed separately.

- Based on the result of converting non-regular employees into regular employees (including indefinite-term workers), the personnel expense budget for the converted employees will be compiled by transferring the personnel expense budget for non-regular employees included in the existing business expenses and miscellaneous salaries, and reducing the transferred amount from the existing business expense budget.

uating the “total personnel expense increase” indicators. The target is within the rate of increase of total personnel expenses based on the “2017 Guidelines for Budget Compilation in Government-Owned Corporations and Quasi-Governmental Institutions”. A full mark is given if the budget is increased within the target limit and 0 if the budget increase exceeds the target limit.

According to the 2017 Guidelines for Budget Compilation, the budget for total personnel expenses shall be compiled by increasing the 2016 budget for total personnel expenses within 3.5%. However, if the 2015 average wage per person for regular employees (including indefinite-term workers) is not higher than 90% of the industry average and not higher than 60% of the public sector average, the budget increase shall be made within 5.0%; if it is not higher than 90% of the industry average and not higher than 70% of the public sector average, the budget increase shall be made within 4.5%; and if it is not lower than 110% of the industry average and not lower than 120% of the public sector average, the budget increase shall be made within 2.5%.

Therefore, it may be necessary to re-examine the existing guidelines for budget compilation standards and revise the current standards for wage increase or provide special rules for exceptional cases in order to offer institutional opportunities to increase the exceptionally low wages of workers of subsidiaries to an appropriate level. Also, when it is inevitable that the employees of both parent institutions and their subsidiaries perform similar/same jobs, it is necessary to stipulate a recommendation to pay salaries to workers of subsidiaries of at least 80% of those paid in their parent companies.

### (2) Reforming the Wage System

Owing to the traditional seniority-based wage system in Korea, the determination of wages is often influenced by age and the number of service years, making it difficult to stick to the principle of equal pay for equal work. Under the

seniority-based wage system, individuals performing a similar job may receive varying wages depending on the years of service, and such gap is particularly pronounced in the public sector. Therefore, it is desirable to shift the current wage system for parent institutions and subsidiaries in the public sector to a job-based wage system that promotes the principle of equal pay for work of equal value.

Under a job-based wage system, while minimizing the wage gap resulting from personal factors such as age, service years and work experience, the method of setting wage difference based on objective factors such as relative value of jobs is used. In short, under the vision of the Moon Jae-in administration's 5-Year Roadmap for Job Creation, the fairness of wage should be improved by firmly adhering to the principle of equal pay for work of equal value and reinforcing the link between effort, performance and compensation. When such a job-based wage system is firmly established, it can also effectively control various fair trade issues (such as excessive service fees) that may arise when using negotiated contracts.

### 3) Employment

#### (1) Principle of Direct Hiring

In principle, direct hiring is the most effective means of protecting workers' employment. However, it should be noted that this paper discusses hiring through subsidiaries based on the assumption that it is inevitable for various reasons; and that hiring through subsidiaries should not be used as a strategic means to avoid direct hiring. Until now, most subsidiaries in the public sector have been established to carry out projects or services of parent institutions – previously carried out by temporary agency workers or workers provided by contract firms. Therefore, in the case of independent business maintained by public institutions in the form of direct hiring, it is desirable in principle to prohibit externalizing such business by hiring through subsidiaries.

#### [5-Year Roadmap for Job Creation]

- (Temporary Agency Workers, Workers Provided by Contract Firms) Determine whether to directly hire or hire through subsidiaries based on the consideration of the size and the characteristics of organization (convert status upon expiration of employment contract); opt for direct hiring for jobs dealing with life and safety of people

#### (2) Securing Employment Stability

Basically, the employment stability of workers of subsidiaries in the public sector is guaranteed when the sustainability, expertise and efficiency of the subsidiaries are secured, but each subsidiary should come up with an independent way to secure employment stability for its employees. To this end, efforts on the part of subsidiaries to enhance the independence of operation, expertise, as well as the sustainability of business management are essential even if they are functioning as subcontractors.

In addition, the public institutions that are in subcontract transactions with the subsidiaries may share part of the responsibilities related to the employment stability of workers of the subsidiaries, or conclude a joint agreement (stipulating the obligation of employment succession at the change of service providers) as part of their mutual efforts and institutional arrangements to promote greater employment stability for workers of the subsidiaries. Such an agreement is helpful because it can prevent the termination of certain subcontract transactions between a public institution and its subsidiary from leading to the job loss for the employees of the subsidiary.

#### (3) Eliminating Factors of Illegal Use of Agency Workers

Even if parent institutions and their subsidiaries are in a principal contractor-subcontractor relationship, the subsidiaries should consider ways in accordance with labor laws to develop into a professional enterprise without



being subordinated to the parent institutions; and the first step towards such development should be eliminating the factors of illegal use of agency workers in their operation.<sup>4)</sup>

Operational independence must be secured in order to eliminate the factors of illegal use of agency workers in the operation of subsidiaries. One way of maintaining independence is to mitigate the exclusiveness of their affiliation with specific institutions. In other words, even a subsidiary belonging to a specific institution needs to actively seek opportunities to improve business expertise by starting business relationships with other public institutions rather than having an exclusive relationship with its parent institution. Doing so can be of great help in maintaining the employment stability of the workers of subsidiaries.

Of course, the fact that a subsidiary maintains an exclusive business relationship with one public institution does not mean that it lacks operational independence. In this case, the affairs of the subsidiary should be specifiable and distinguishable from the other tasks of the public institution.

If there is a high correlation between the work of subsidiaries and their parent institutions, the parent institutions are likely to exercise supervision and issue orders to the employees of the subsidiaries. The possibility is higher if the work performed by the employees of the subsidiaries is directly linked with the quality of the goods or services of the parent institutions. Thus, if the work of subsidiaries is directly connected with or closely related to the work of parent institutions, it is recommended to avoid the establishment of subsidiaries in principle. In such cases, it would be desirable for the parent institutions to hire workers directly.

#### **IV. Conclusion: Business Independence and Autonomous Labor Process**

So far, we have summarized the issues related to hiring through subsidiaries, which is one of the types of hiring available in the course of regularizing non-regular jobs in the public sector. It is true that under the existing approach of operating subsidiaries in public sector, subsidiaries were not free from the control of their parent companies in terms of governance, and faced some negative issues such as their wages being lower and working conditions being poorer compared to those offered at their parent institutions. In order to address such negative image of subsidiaries in the public sector, it is necessary to establish them not with the purpose of externalizing high-risk or labor-intensive jobs or reducing costs but to operate them as professional agencies to perform specialized tasks. In the case of existing parent institutions, they have unique functions and their employees should focus on performing the core tasks surrounding such functions. As for the additional tasks other than these core tasks, it would be more efficient in terms of strategic operation and personnel management to give such tasks to other agencies specialized in their respective field.

To this end, some of the prerequisites mentioned in this article will need to be fulfilled. First of all, it is necessary to ensure that subsidiaries are able to maintain their business in a stable manner by improving the legal grounds for using a negotiated contract. Currently, the government is revising the related legal system. Also, subsidiaries need to acquire operational independence to a certain degree instead of being indirectly controlled by their parent companies as they are now. To do so, it seems that institutional mechanisms such as the worker-director scheme or the

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4) "As can be seen from the investigation into illegal dispatch of KTX crews belonging to Korail Tourism Development Co., the lack of business independence on the part of a subcontractor as it carries out the duties that are systematically linked with the business of a principal contractor has resulted in a structure under which the subsidiary is under the direct control of the principal contractor in its business management. Consequently, the subsidiary functions in effect as a window to supply low-wage workforce to its principal contractor while performing ancillary functions for the principal contractor without having independence in its business functions (Nam Woo-geun, 2017:14)."



Parent-Subsidiary Joint Labor-Management Council need to be introduced. In addition, in terms of wages and other working conditions, it will be necessary to avoid excessive wage gap with the parent institutions and to establish a wage system that promotes the principle of equal pay for work of equal value. In terms of employment, further efforts need to be made to secure employment stability and to eliminate the factors of illegal use of agency workers.

Even when establishing subsidiaries as a means of converting non-regular workers into regular workers in the public sector, it is essential to ensure they have business independence and expertise as well as the rationality of business execution and independent management of labor

process. According to the requirements contained in the guidelines for regularizing non-regular jobs in the public sector released by the Ministry of Employment and Labor, there exists “the need to design and operate a business management system and a personnel management system so that subsidiaries can provide better services and function as a professional business organization”. If such requirements are not met or cannot be met in the future, it would be desirable not to opt for hiring through subsidiaries. For professional management, subsidiary companies must be able to accumulate their own expertise and technical skills and to self-procure the necessary equipment and materials such as specialized equipment.