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The Future of Contractual Mandatory Retirement in South Korea

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The future of contractual mandatory retirement in South Korea*

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Abstract

Although contractual mandatory retirement at a specified age has been eliminated, or limited, in many Western nations, the practice remains widespread in other parts of the world. In South Korea (henceforth, Korea) most workers are subject to contractual mandatory retirement, often while still relatively young; that is, in the 50s. Korean retirement policies are deeply rooted in the belief by policy makers, employers and unions that mandatory retirement creates jobs for young workers. In addition, because worker compensation is linked to age, employers argue that the seniority-based wages paid to older workers are excessive. Notwithstanding the opposition to reforming retirement policies, Korea faces a rapidly aging population that will require modifications to existing retirement arrangements. Moreover, greater emphasis on human rights, and efforts to reduce age-based discrimination in employment, will add to the pressures to increase the age of contractual mandatory retirement.

Keywords: *Mandatory Retirement, South Korea, Age Discrimination, Population Aging*

JEL classification: *J26, J14 and J78*

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Executive Summary

In the past several decades a number of Western nations, including Canada, the United Kingdom and the United States have eliminated contractual mandatory retirement. Most Western nations have sought to extend working lives in light of demographic trends and pressures from an aging population on welfare state programs. In many non-Western nations, contractual mandatory retirement is still widespread, and particularly so in East Asia. In South Korea (henceforth, Korea) nearly all workers face contractual mandatory retirement, many at young ages; such that the average retirement age is 55. Most of those who are retired are forced to stay in the labour market, primarily in low-paying and precarious employment in the service sector or as small entrepreneurs, where many remain until their late 60s or into their 70s.

Notwithstanding that economic theory suggests – and that the experience of other nations reinforces – that mandatory retirement does not create jobs for youth, most policy makers, employers and unions in Korea believe that there is a direct connection between mandatory retirement and youth employment. Moreover, because most firms have seniority-based wages, and because workers are hired and promoted as a cohort, employers argue that the wages of older workers exceed their contribution to the firm.

Korea’s population is aging rapidly, and this, among other factors, has recently generated debates on contractual mandatory retirement. Although most workers approaching contractual mandatory retirement ages express a wish to remain with their employer (even at lower wages), no consensus has emerged among employers, labour and government.

The analysis of this paper suggests that altogether eliminating, or at least increasing, contract mandatory retirement in Korea would not have significant labour market or workplace impacts. That older workers are willing to accept limits on compensation implies that a mutually agreeable trade-off between workers and employers is possible. However, there are barriers to legislative reforms because age-based distinctions are deeply rooted in employment practices and workplace arrangements in Korea.

The growing attention to discrimination in employment, including that which is age-based, may provide an opportunity to some retirement reforms to occur. In any case, the demographic trends, and shifts in the labour market from manufacturing to service employment, mean that retirement policies will need to be reformed in the short and medium term.

The scholarly literature and the experience of other nations point to two possible roads for Korea. One involves incremental reforms of contractual mandatory policy, while the other entails a wide-ranging increase of legislated retirement ages, with a timetable to eliminate the practice altogether. While the second option is less desirable for employers, who will always prefer to determine retirement ages rather than have this set by government, such an approach is no less risky than the first in allowing necessary adjustments in response to demographic trends and labour market shifts.

The future of contractual mandatory retirement in South Korea

Introduction

In the past 25 years a number of nations have largely banned contractual mandatory retirement. Most notably, the United States did so in 1980s, followed by Austria, New Zealand, Canada, and most recently in 2001, Great Britain. However, contractual mandatory retirement remains a common feature of labour markets in parts of the world, most notably in East Asia. This paper analyzes contractual mandatory retirement in South Korea (henceforth, Korea), with a focus on the policy debates occurring in that country, which faces a rapidly aging population.

Retirement is a complex social institution. For individuals, it represents a significant event in the life cycle and affects the workplace, the labour market, and the economy. When many individuals retire within a relatively short time, or when there are significant labour market or public policy shifts, as is the case in an aging society, retirement becomes a major public policy issue (Yang & Klassen, 2010).

Among industrialized nations there is considerable variation in policies regarding retirement and the associated income-security schemes (Lynch, 2006, pp. 15–43). With regard to retirement-related policies, and particularly retirement ages, each nation has its unique set of institutional arrangements and policies (Cooke, 2006; Fornero & Sestito, 2005; Kim, 2009).

Extending working lives is a policy objective of governments in many developed nations (Organisation for Economic Co-operation and Development [OECD], 2006; Taylor, 2004). Delaying the age of retirement is necessary to cope with aging populations, longer life spans, and lower fertility rates, as well as with limited state funds for income security and health programs for those no longer in the labour force.

Whereas governments in most Western nations seek to delay retirement, Korean policy makers, employers, and workers face a situation in which workers already have long working lives, but, paradoxically, also face early retirement from their main lifetime job. As such, the Korean government and its social partners must undertake a more fundamental restructuring of labour market policies in response to an aging population.

In Korea, as is also the case in some other East Asian nations such as Japan, retirement policies and patterns are quite different from those of most other OECD nations.

The distinguishing feature for many workers in Korea is contractual—and often involuntary—retirement from one's main job at a young age, followed by a second career in self-employment or contract work. The contractual retirement age, found in almost all employment and union contracts, varies from occupation to occupation. It is 65 for university professors, 61 for teachers, 60 for civil servants, lower in the public sector (58 in the financial-services sector), and even lower in the manufacturing sector.

In some sectors and companies, workers are habitually forced—through the use of both formal and informal mechanisms—to retire years before their contractual retirement age. In the financial-services sector it is common for workers to retire in their early 50s. This is done through "honourable retirement" and "early retirement" and by other mechanisms, such as shifting workers to undesirable jobs. After contractual mandatory retirement, workers must continue to do paid work in order to avoid becoming poor, especially given long life spans and a small welfare state (Yang, 2011a).

Although contractual mandatory retirement is universal in Korea, it is not necessarily accepted by workers. Indeed, the relatively young retirement age, along with the non-voluntary and ageist nature of retirement, results in low levels of life satisfaction, especially when compared with the experience of workers in Western nations (Shin, 2007; Yang, 2011b).

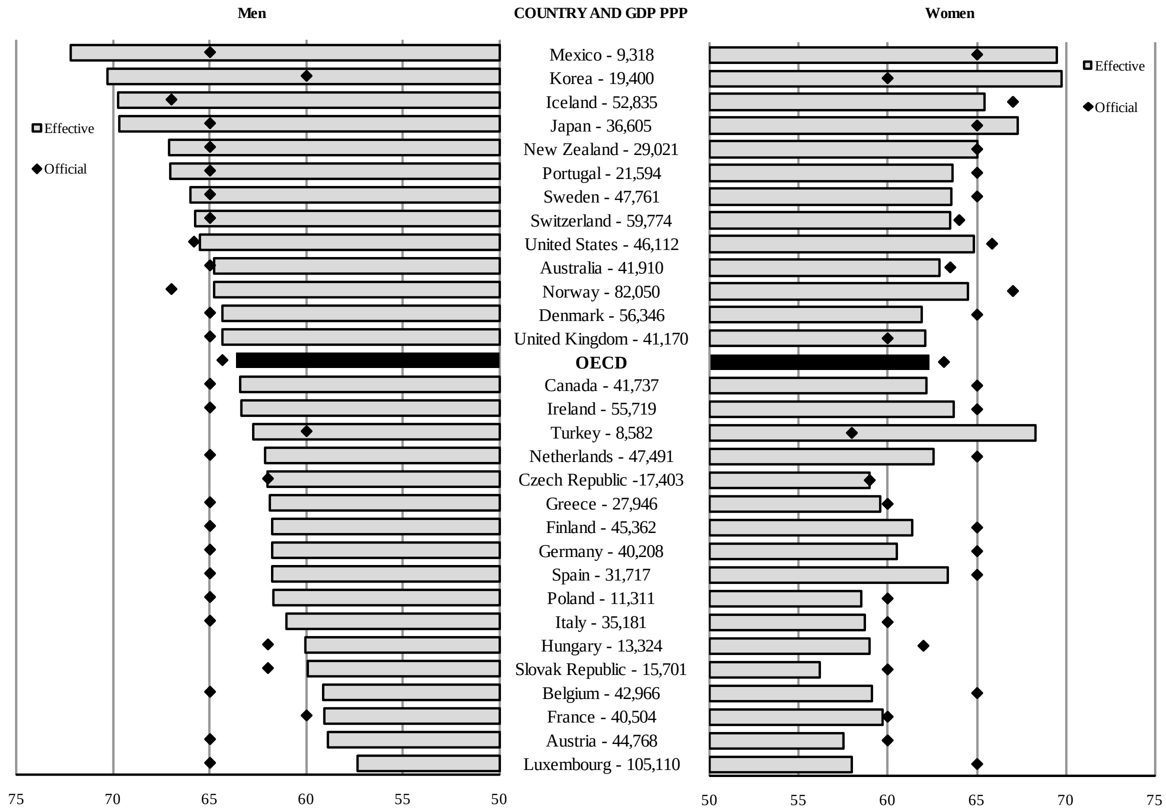
The conditions that have historically supported early contractual mandatory retirement, by maximizing its benefits and mitigating its problems, have changed in the past decade. Broad demographic trends such as rapid population aging, increases to life expectancy, and continuing low fertility are having an impact on the labour market. At the same time, the economic sectors crucial to the export-driven competitiveness of the economy are shifting from manufacturing to services.

At the level of employers, human resources management practices are being altered to resemble those of Western firms, including greater emphasis on (individual) performance-based systems (Kim & Briscoe, 1997; Lee & Lee, 2003). Unions are beginning to view increasing contractual mandatory retirement ages as a concern for many workers (Korea International Labour Foundation [KOILAF], 2010a, 2010b). The rise in female labour force participation—along with other factors—has resulted in a greater recognition of individual rights in Korean workplaces, especially with regard to gender (Cho, Kwon, & Ahn, 2010). Last, state policy has shifted, too, for example, by gradually raising the age of eligibility for the National Pension Scheme from 60 to 65, which will further widen the gap between the age for pension eligibility and the age for contractual mandatory retirement.

The objective of this paper is to analyze how the experience of other nations can be applied to Korean policies on contractual mandatory retirement. The paper is composed of two major parts. The first is a review of economic theory and the experience of other nations, primarily those in the OECD that have increased the age for contractual mandatory retirement, or eliminated it altogether, so as to reduce the number of years that workers spend in so-called second careers. This allows for evidence-based analysis later in the paper. The second part of the paper analyzes the extent to which reforms to existing Korean contractual mandatory-retirement practices and policies might be undertaken.

Review of the Experience of Other Nations

Retirement policies and practices – including contractual mandatory retirement – arose in many nations during a time when labour market and economic conditions were quite different from those found today. As shown in Figure 1 below, there is no discernable pattern between retirement patterns and the economic performance of a nation. Some countries such as Mexico have high ages of retirement (over 72 for men) and low GDP, but some like Sweden also have relatively high ages of retirement (over 66 for men) but have high GDP. Alternatively, some countries, such as the Slovak Republic have low retirement ages (60 for men) and low GDP, while other countries, such as France also have low retirement ages (59 for men) and high GDP. In most countries, the age of eligibility for full pensions is higher than the effective retirement age; in other words, workers generally retire before the normal pensionable age. A small number of countries have pension eligibility ages below actual retirement ages; in other words, workers generally continue to work even though they might be eligible for (some) pension income. The variation in retirement age and GDP in Figure 1 suggests that retirement ages are not particularly correlated with labour market and economic performance.



Note: Effective retirement age shown is for five year period 2004-09; Source: OECD, updated from OECD (2006).
Pensionable age is shown for 2010.
GDP data is an average of four years (2006 to 2009) in current US dollars
GDP data from World Bank: http://data.worldbank.org/indicator/NY.GDP.PCAP.CD
adapted from: *Pensions at a Glance 2011: Retirement-income Systems in OECD and G20 Countries*, OECD 2011

Figure 1. Average effective age of labour-market exit, normal pensionable age and country GDP at PPP (2004-1010)

During the past several decades, a number of nations have eliminated contractual mandatory retirement. This was typically done because of changes in demography and the labour market, as well as the view that contractual mandatory retirement was a form of discrimination. This section reviews the experience of five nations: the United States, Australia, Canada, Britain and Japan.

United States

In the United States, federal legislation in 1978 banned contractual mandatory retirement before age 70. In 1986, mandatory retirement was eliminated altogether, except for university professors, for whom it was removed in 1994. The experience of the United States indicates that the removal of mandatory retirement does not create dysfunctions at either the level of the individual workplace or more broadly with the economy. Indeed, researchers have proposed that the greater flexibility in making decisions about retirement in the United

States allows that nation to better address economic and social challenges by continuing to draw on the productive efforts of older workers (Gillin & Klassen, 1995).

Australia

Beginning in 1990, states in the Australian Commonwealth began abolishing compulsory retirement and including age in their antidiscrimination legislation. By 2001 all states and territories (excluding the sparsely populated Northern Territory), as well as the Commonwealth government, had removed compulsory retirement for their own workers as well as for most industries.

There is no indication in the academic literature or the public policy discourse that these changes have had detrimental effects on Australian productivity, unemployment rates, or other social or economic conditions. A review of industry publications finds no evidence that the ban on mandatory retirement has been problematic, has increased costs, or has had undue negative effects. Instead, the ban has been accepted and has become part of doing business.

Canada

Contractual mandatory retirement was largely eliminated in Canada between 2006 and 2009, although two provinces (Quebec and Manitoba) had abolished it during the 1980s. Private-sector workers under the jurisdiction of the federal government—approximately seven percent of the work force—continue to face mandatory retirement, although the federal government is planning to end this practice. As in other nations, not all employers were initially supportive, and unions were generally opposed; however, once mandatory retirement was banned, there has been no opposition or problems (Gillin, MacGregor, & Klassen, 2005). Again, as in other nations, seniority-based pay schemes such as those in universities continue to exist. Last, and as is the case with the other nations, retirement patterns have not undergone significant shifts.

United Kingdom

Mandatory retirement was eliminated in the United Kingdom in April 2011. Prior to this, from 2006 to 2011, 65 was the mandatory age for retirement. Before 2006, employers were able to determine a contractual retirement age, with most setting an age between 60 and 65. As in the other nations that have abolished fixed retirement ages, some groups of workers continue to face contractual mandatory retirement, such as those in public-security and safety occupations. Employers can, if shown to be “objectively justified,” impose a fixed retirement date, but few in the private sector have done so.

Last, as with the other Anglo-Saxon nations reviewed, the government considered the constitutional (human) rights of older workers. All the Anglo-Saxon nations have a tradition, strongest in the United States, of enshrining equal opportunity in the workplace, and of preventing discrimination based on individual characteristics such as gender, family status, and age.

Japan

Japan’s labour market resembles that of Korea: a rapidly aging population, seniority-based wages, and contractual mandatory retirement at a relatively early age (but later than Korea). As in Korea, companies in Japan have used informal methods to persuade workers to retire at ages younger than those specified by employment contracts. And, as in Korea, employers and cultural norms are averse to having younger workers supervise older workers (Lincoln & Nakata, 1997).

A contractual mandatory retirement age in Japan of 55 was well in place prior to the Second World War, when life expectancy was shorter (Martin, 1982, p. 33). Starting in the 1970s and for more than two decades, Japanese policy makers sought to increase the age to 60 with only limited success; ultimately public and political pressure were needed to institutionalize the retirement age at 60 in the 1990s, where it effectively has remained since and seems likely to remain for the foreseeable future.

In summary, Japan has adopted a gradualist approach to increasing its retirement age, driven primarily by the interests of large employers. Given the stagnant rate of economic growth in Japan during the past two decades, it is difficult to argue that Japan is necessarily a successful model of coping with an aging workforce.

Labour Market Performance

Public policy debates about mandatory retirement in countries that continue to have fixed retirement ages revolve around the extent to which banning contractual mandatory retirement influences labour market performance. Three relationships are at the core of this debate. First is the relationship between youth unemployment and older workers remaining longer in employment positions; second, the relationship between age and productivity; and third, the relationship between age and compensation.

Fortunately, over the past decades economic theory and empirical research on the effects of contractual mandatory retirement, and its elimination, on the labour market and workplace has addressed these relationships. Below is a review of each of these relationships, with a focus on both the theory and the experience.

Youth Unemployment and Older Workers

It is now well recognized that banning mandatory retirement will not create employment positions for young people in the economy as a whole. To argue otherwise is the lump of labour fallacy—that there are a fixed number of jobs in the economy. Although appealing from a commonsense perspective, limiting employment opportunities for some workers—such as older people or females—will result in an overall decrease in economic activity and a decline in the total number of jobs in an economy.

The OECD (2006) stated that "It is important to dispel a number of myths . . . for example, the claim that fewer jobs for older workers results in more jobs for younger workers, though unfounded, is proving especially stubborn" (p. 13). Recent analysis from the OECD (2011), as illustrated in Figure 2, shows that the employment rates for younger and older workers are positively correlated and highly significant in statistical terms; as one increases so does the other. As such, the OECD (2011) concludes, "The idea that public policy can re-shuffle a fixed number of jobs between workers of different ages is simply not true" (p. 76).

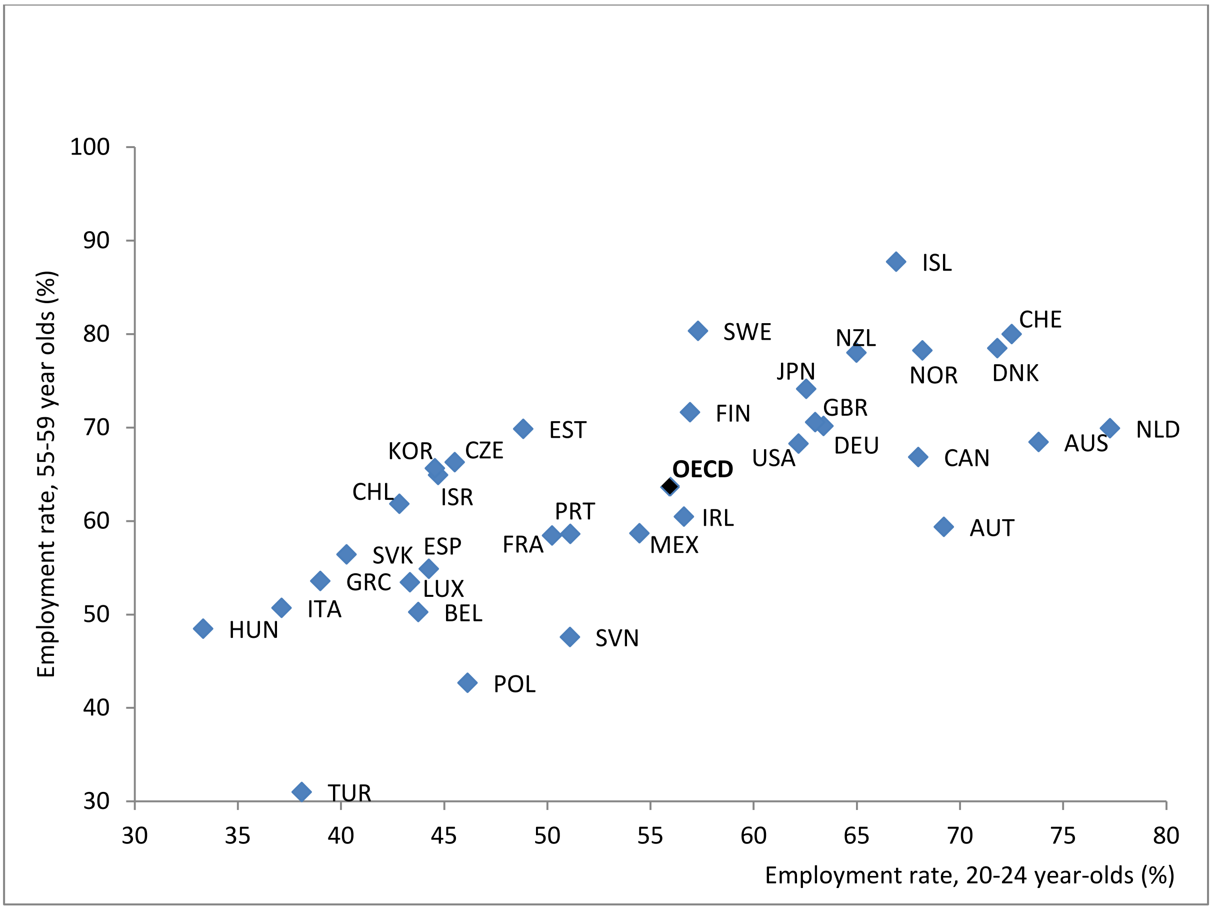


Figure 2. Employment rates for individuals ages 55–59 and 20–24 years OECD nations (2009).

Reprinted from Figure 4.6 in *Pensions at a Glance 2011: Retirement-Income Systems in OECD and G20 countries*, by Organisation for Economic Co-operation and Development, 2011, Paris: Author.

All nations that have eliminated mandatory retirement altogether, or that have increased the retirement age, have seen no increase in youth or total unemployment rates. Rather, unemployment and labour market participation rates are a result of broader economic and demographic conditions.

It should be noted that in all economies—whether they have contractual mandatory retirement policies or not—the unemployment rate for youth is higher than for older workers; a trend that has not changed in many decades. If youth unemployment is deemed a problem, then there are other policy levers, including education and training policies, which can address the problem more effectively than contractual mandatory retirement (OECD, 2007).

Age and Worker Productivity

The productivity of older workers has been subject to a long-standing and extensive study in the academic literature. The landmark review of job performance and aging in 1983 found inconclusive results, noting that no generalizations can be reached, with the exception that older workers have difficulties in those rare, and disappearing, jobs that required maximal levels of physical exertion (Doering, Rhodes, & Schuster, 1983). Meta-analyses (studies that summarize the findings of many previous studies) of the relationship between age and job performance have found an average correlation close to zero (Martocchio, 1989; McEvoy & Cascio, 1989). A review of past research noted that “the best conclusion that can be made regarding the relationship between age and performance is that there is no consistent relationship across settings” (Farr, Tesluk, & Klein, 1998, p. 149).

There is no evidence that any specific age marks the beginning of a decline in work-related abilities for any group of workers. The extensive research to date demonstrates that specific individuals, occupations, economic sectors, and workplaces have unique characteristics that accommodate older workers, which must be examined and taken into account.

The experience of other nations is that once mandatory retirement is eliminated or the retirement age increased, it is typically the most motivated, and productive, workers who elect to work longer. This, on its own, ensures that there is no loss of productivity even as older workers remain employed longer.

Age and Worker Compensation

One argument in support of mandatory retirement made by some economists is that older workers are paid more in compensation than their current worth (or productivity) to the firm. In other words, workers, especially those in a workplace with a seniority system, are underpaid when young and early in their careers, and then are paid more than their economic contribution later in their careers, thus justifying being retired at a fixed age (Lazear, 1979). However, for the deferred-compensation argument to hold explanatory power, all workers must be hired at a very young age, receive training only in their first few years, and continue to work in the same manner and with the same technology as when hired, in employment/union contracts that never change, and equally productively. Furthermore, employers must not have any means to terminate employees other than to wait for them to reach the age of contractual mandatory retirement (Kesselman, 2005).

It may also be the case that mandatory retirement causes lower productivity among older workers. If firms and individuals know that employment termination is imminent, there is little incentive for investment from either party in training and other forms of human capital development. The complete withdrawal from employment, and other associated costs (such as greater state expenditures for individuals not in the labour force), are not included in Lazear's (1979) model. Indeed, Lazear's model assumes that workers move from employment earnings to pension earnings, which is not the case in some countries, including Korea. In short, contractual mandatory retirement may be rational for some firms in particular conditions, but not for the economy as a whole.

Although typically employers argue that older workers are overpaid relative to their productivity, there is little empirical evidence of this. Even if this is the case, there are options—other than mandatory retirement—for addressing the situation, such as additional training for older workers, retirement incentives, wage subsidies for older workers, the renegotiation of salary, peak salary schemes, and performance-based compensation schemes.

Summary

The tenets of economic theory are borne out by the experience of other nations during the past 25 years. The removal of contractual mandatory retirement has had little or no discernable impact, notwithstanding opponents (usually employers) having predicted major negative effects. Mandatory retirement has been completely eliminated, or its age increased, in a number of countries over the past two decades. There is no evidence that younger workers have been disadvantaged, that productivity has suffered, or that compensation levels have harmed employers. Thus, the empirical evidence is clear that removing contractual mandatory retirement has not resulted in dysfunctional effects.

The Korean Case

The experience of other nations is a useful starting point from which to analyze Korean policy with regard to contractual mandatory retirement. Korean public policy attention to retirement, and specifically contractual mandatory retirement, is recent. It was only in 2006 that concerted attention was paid to the labour market participation of middle-aged and older workers with a tripartite agreement to increase participation rates. Previously, labour market policy focused on responses to economic crises, labour relations, and active labour market measures (Yang, 2010, Table 2).

In analyzing contractual mandatory retirement policies in Korea, four key aspects of workplace and labour market arrangements are studied: (a) working lives, (b) worker preferences, (c) seniority-based wages, and (d) human rights. These were selected because they feature most prominently in public debates on contractual mandatory retirement in Korea and are critical in shaping policy responses.

Working Lives

Working lives in Korea are among the longest in the OECD nations, with the average age of retirement slightly above 70. The labour market participation rate of older workers has remained high and stable for the past 5 decades. In 2005, 50% of men ages 65 to 69 were in the labour market, whereas 34% of those over 70 remained in the labour force (C. Lee, 2010). More recent figures reveal that in 2010, 36% of those 65 to 79 were in the labour force (Korea National Statistical Office, 2010).

Working lives are long, in large part, because pension income after contractual mandatory retirement is low. In 2010, slightly less than half (46%) of those 55 and older reported receiving pension income, and of those who did have such income, 85% received less than 500,000 won per month (Korea National Statistical Office, 2010).

Worker Preferences

Recent survey research found that the majority of Korean workers (59%) are willing to accept a reduced salary for an opportunity to work past their retirement age (Korean workers willing to work under salary peak system, 2011). Of those, 55% expressed a desire for a four to five year extension of employment, with 37% willing to take a salary cut of up to 20% (Korean workers willing to work under salary peak system, 2011).

In 2010, the Federation of Korean Trade Union (FKTU), one of the two large labour federations, supported increasing the contractual mandatory retirement age to 60. The FKTU's rationale was that such an extension would assist in addressing population aging and provide greater financial security for older workers (KOILAF, 2010a, 2010b).

Individual unions, rather than union federations, have expressed a less clear stance on mandatory retirement because they are the locus of an intergenerational schism. Younger union members typically support mandatory retirement, believing that it creates opportunities for their advancement in the firm. Older workers, as discussed above, wish to see contractual mandatory retirement eliminated, or at least the age extended. As one union official noted, “the young–old tension [in his union] represents a special challenge” (personal interview, Seoul, July 13, 2011). Indeed, academic research “suggests that the labour unions may tacitly approve” of mandatory-retirement practices (Cho & Kim, 2005, p. 298).

Individual workers, especially those who are older, are constrained to challenge the existing regime for fear of appearing to be selfish. As a manager in a large firm in the financial-services sector noted, “Most colleagues in my company want to work longer [than age 55], but they cannot speak out” (personal interview, Seoul, April 2, 2007).

In summary, there is no doubt that many workers prefer an increase in the mandatory retirement age. As workers reach the mandatory retirement age, they are more likely to wish to work past this age at their main job, and to be willing to accept a reduction in employment income to do so.

Seniority-Based Wages

Seniority-based wages are seen by employers as the main barrier to increasing the age of contractual mandatory retirement. Seniority-based wages in Korea mean that all those hired in the same year by a firm—who are usually all the same age—are given identical pay increases each year. The cohort is also promoted as a group, especially since workers do not want to report to someone who is younger. Employers argue that the wages of older workers are greater than the workers’ contribution (productivity) to the firm, and that mandatory retirement is the only means of dealing with the discrepancy.

However, “honorable retirement” (early retirement with a lump-sum payment of one to two times annual salary) practices do provide employers with the ability to terminate workers with low performance at any age (Yu & Park, 2006). As such, the notion that employers must wait for workers to reach contractual mandatory retirement is not completely accurate. Of course, “honorable retirement” is also used to terminate older workers, but a more limited application of this practice provides employers with the means to remove workers with chronic low performance and to respect seniority-based wages.

Group harmony (“in-hwa”) and teamwork are core features of Korean workplaces (Kim & Briscoe, 1997). These features, according to many employers and unions, are supported by seniority-based wages. Yet, there is no reason why harmony and teamwork cannot be retained in the absence of contractual mandates.

Human Rights

Notwithstanding the many societal and labour market changes in the past decades, age discrimination in the form of contractual mandatory retirement persists. There are no laws in Korea that prohibit setting a retirement age, and retirement is not considered age discrimination (Shim, 2010). Korea is the only OECD nation that does not legislate a minimum mandatory retirement age, leaving employers with the freedom to set nearly any age, no matter how low.

Age-based distinctions are deeply rooted in employment practices in Korea, and especially in determining layoffs and retirement (Chang, 2003). For instance, Korean laws classify those 55 and older as "aged" and those 50 to 55 as "semi-aged," notwithstanding that individuals in these ages generally are as healthy as younger people (Hong & Lee, 2011). The National Statistical Office and others define "old age" as beginning at age 55.

There are signs that age discrimination is becoming a broader public policy concern, which should be expected in a rapidly aging population. The National Human Rights Commission established in 2001 has ruled on a number of cases on mandatory retirement and established the principle that an organization must justify the practice of having different retirement ages for different groups of workers. Although the rulings of the commission are only in the form of recommendations, they have had some influence on public-sector employers. For example, because of the commission's rulings, the government has replaced the previous retirement ages of 58 for lower-ranked workers and 60 for higher-ranked workers with a uniform retirement age of 60 (personal interview, Seoul, July 21, 2011).

Since 2005, with the introduction of affirmative action requirements for employers, gender discrimination has received greater attention from employers, resulting in some improvement in the status of women in the workplace (Cho et al., 2010). The focus on gender discrimination has not yet translated to age discrimination, but this may yet happen. The 2008 Korean Age Discrimination in Employment Act prohibited hiring decisions based on age. Its passage represents recognition that age-based distinctions in the workplace are discriminatory, and it is not a significant leap to argue that if age-based hiring is illegal, age-based retirement should be illegal as well.

In summary, mandatory retirement involves making a decision about employment based on a single characteristic—age—that is unrelated to workplace performance. The trend in Korea is toward greater attention to human rights and to policies that avoid discriminating against groups of people in workplace relationships due to gender and (with regard to hiring) age.

Conclusions

There has been a transformation of the Korean labour market in the past three decades, including increased participation of women in the labour force. Moreover, there has been a broader transformation of economic activity, including the rise of the service sector and the use of new technologies. Last, there have been dramatic shifts in Korea's demographic structure, including a changing life cycle, longer life span, low fertility, and rapidly aging population. Throughout these extraordinary changes, contractual mandatory retirement has remained largely unaltered. It is widely understood by all observers and by the labour market participants (employers, labour unions, and government) that this cannot continue and that reforms must be enacted. However, the nature and speed of reform remains under debate, and the key groups—employers, labour, and government—fail to agree on a strategy (Economic and Social Development Commission, 2011).

The academic literature and the experiences of other nations point to two possible roads for Korea. The first are incremental reforms of contractual mandatory retirement policies and of seniority-based compensation schemes dictated by large employers and driven by the specific economic and labour conditions of individual economic sectors. This is, in effect, the current policy direction and what is usually recommended by experts and observers (see Chang, 2011; Phang, 2011). This is the approach the government is currently taking, which mirrors to some extent the strategy used by Japan.

The second approach is a legislative reform of contractual mandatory retirement that increases contractual mandatory-retirement ages with a timetable to eliminate it altogether, along with legislation to limit seniority-based wage compensation. This approach assumes that unions and employers will not reach a satisfactory consensus and that the quick elimination of mandatory retirement will foster productivity growth (by curbing the low-value-added small-services sector) and other labour market reforms, particularly in the context of a rapidly aging population. This approach also assumes that the current arrangements create unnecessary conflict—such as between younger and older workers—and prevent the labour market adjustments required for an aging population.

Arguably, the second approach is less desirable (at least initially) for the private-sector parties: many employers and some workers. However, the experience of other nations, and the evidence from economic theory, is that such an approach may be less risky than the incremental advances. Given the stagnant economic growth of Japan in the past several decades, it is difficult to argue that its model of incremental reform dictated by large employers is particularly attractive.

And, indeed, some Korean experts have begun to call for immediate increases to the contractual mandatory-retirement age (Choi, 2009; K. H. Lee, 2010; Suh, 2011). For several years, the OECD has been recommending the abolition of the mandatory retirement system in Korea (OECD, 2008). Most recently, the OECD (2010) has stated, “One priority [for public policy] is to require companies to set a mandatory retirement at an age closer to the pension eligibility age—or forbidding the use of mandatory retirement altogether—thereby helping to change the seniority-based system” (p. 40). Other experts have proposed how adjustments to seniority-based compensation are possible in the context of higher retirement ages (Phang, 2011).

An increase in the retirement age, and its ultimately abolition, is unlikely to occur naturally with the social partners finding consensus. Private interests, especially employers, will always prefer contractual mandatory retirement, because its benefits are retained by the firm, whereas its substantial costs are borne by the state and by individuals. It is this tension that Korean policy makers will need to resolve in the soon given a rapidly aging population. In doing so, Korea need not necessarily emulate other, but has an opportunity to forge its own model based on its unique institutions and conditions.

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