

## RECONSTRUCTING THE GERMAN SOCIAL MODEL

by Gerhard Bosch

---

After WW II, the previously rather rudimentary German social model was developed into an inclusive Bismarckian welfare state that protected the vast majority of the population from life's main risks. In the past 20 years, the social security system has been reorganized at a rapid pace. The hitherto inclusive wage system has been eroded by the deregulation of product markets and the Hartz laws with negative spillover effects for all wage-related benefits of social insurance especially pensions. Therefore the German welfare system has become more exclusive. At the same time, the reform of the traditional German family model has begun with the development of child care and all-day schools and the introduction of the parental allowance. In addition a mandatory long-term care insurance was introduced and the modernisation of dual system of vocational training helped to reduce youth unemployment.

Dopo la Seconda guerra mondiale, il modello sociale tedesco, in precedenza piuttosto rudimentale, si è trasformato in uno stato sociale bismarckiano di tipo inclusivo che proteggeva la maggioranza della popolazione dai principali rischi nell'arco della vita. Negli ultimi vent'anni, il sistema di sicurezza sociale è stato riorganizzato a un ritmo sostenuto. Il sistema salariale, fino ad oggi di tipo inclusivo, è stato minato dalla deregolamentazione dei mercati dei beni e dalle leggi Hartz con ricadute negative su tutte le prestazioni previdenziali legate ai salari, in particolare le pensioni. Pertanto, il sistema di welfare tedesco è diventato più elitario. Allo stesso tempo, la riforma del modello di famiglia tradizionale tedesca ha avuto inizio con lo sviluppo dell'assistenza all'infanzia e delle scuole a tempo pieno, e con l'introduzione del sussidio parentale. Inoltre, è stata introdotta l'assicurazione obbligatoria per l'assistenza di lunga durata, e la modernizzazione del sistema duale di formazione professionale; quest'ultimo ha contribuito a ridurre la disoccupazione giovanile.

---

### 1. INTRODUCTION

In comparative research on welfare states, the German social model is regarded as the archetype of the conservative welfare state, which seeks, through its social security arrangements, to maintain differences in status and to support traditional family forms with a single male breadwinner (Esping-Andersen, 1990). In contrast to the predominantly tax-funded, universalist Scandinavian social model, it is more strongly based on social insurance schemes that, in the Bismarckian tradition, provide cover only for dependent employees. Thus access to insurance benefits, as well as their level and quality, depend

on a worker's position in the labour market. Wives and children are insured through the gainfully employed husband.

However, social insurance schemes constitute only a part of the German social model. Other central pillars of the model are the wage system; codetermination at establishment and company levels; labour law; universal, needs-dependent social assistance and basic social protection; family policy; the redistributive tax system; and the public sector, with its social services organised primarily at local government level. In addition, there is a complex system of fiscal equalization between the *Länder* and municipalities with unequal economic power in order to ensure equal living conditions in all parts of the country.

The extent to which the welfare state helps to avoid, mitigate or compensate for social problems at various stages of the life course can be understood only by examining how these various elements of the German social model interact with each other. In combination with an inclusive wage setting system, social insurance schemes give rise to only slight differences in status and make an important contribution to the reduction of poverty. By the mid-1990s, this inclusive wage system had led to the establishment of a middle class that, by international standards, was broadly based on low levels of income inequality and living standards that were guaranteed by social insurance benefits, even during long periods of illness and unemployment and in old age.

It is on the basis of these institutional complementarities that we describe the German social model of the post-war period as an *inclusive Bismarckian welfare state*. Among dependent employees, the only separate system is for career public servants (*Beamte*). By virtue of this universality, the social insurance schemes offer protection against the main risks (unemployment, sickness, accident, age) to the vast majority of the population, right up to the upper middle classes. The broad protection afforded by the German welfare state also explains its high level of acceptance among the population, also because most of the major social reforms have been introduced by agreement among the major political parties.

In contrast to many other European countries, Germany has not really experienced a dismantling of its welfare state, either in the years following the financial crisis of 2008 or, further back, in the two decades before the financial crisis. Rather, social benefits have been subjected to a combination of cutbacks, development and reorganization. On one hand, important new benefits have been agreed, such as the introduction of long-term care insurance and the parental allowance (*Elterngeld*). Moreover, during the financial crisis and despite a drastic decline in output, job losses have been kept to a minimum through a combination of active labour market policies and a revival of social dialogue. On the other hand, there have also been drastic cuts, particularly in old-age and unemployment insurance, and the labour market has been extensively deregulated as a result of the so-called Hartz Acts of 2004). Moreover, the hitherto inclusive wage system has been eroded by the deregulation of product markets and privatization schemes. Increasing pay inequality has also significantly weakened the positive complementarities between the various elements of the German social model because of the spillover effects for all wage-related benefits of social insurance.

As a result of the cumulative effects of the changes in the social and wage system, there has been a shift away from the inclusive Bismarckian model towards a *dualistic social model* or an increasingly *exclusive Bismarckian model with high income inequality*. In view of the current inflationary use of the term 'dualization', it will be essential to describe precisely the various aspects of this risk.

This article is structured as follows. In Section 2, the development of the German social model in the post-war period is outlined. In Section 3 to 9, the main pillars of the German social model and the changes they have undergone in the past 20 years are analysed, including the Hartz Acts, wages, old age protection, family policy, long-term care insurance and regional fiscal equalization.

## 2. CONSTRUCTION OF THE GERMAN WELFARE STATE AFTER THE SECOND WORLD WAR

It was not until after the Second World War that the welfare state actually began to be developed. It was only then that levels of benefits and universality were attained that justified use of the epithet 'inclusive'. The social benefit ratio, which in 1913 was only 3.1 per cent and in 1938 6.0 per cent of GNP (Teppe, 1977, p. 195), rose by 1950 to 19 per cent, because the massive socio-political problems that arose in the aftermath of the war, such as forced displacements, homelessness, inability to work, unemployment and so on, were much more extensively alleviated than after the First World War. Despite extensive development of the welfare state, the social benefit ratio rose to only 23.3 per cent by 1970, because high growth rates led to disproportionate increases in receipts and the decline in unemployment led to a reduction in expenditure on unemployment benefits. This changed with the first oil crisis in 1973. Unemployment increased and the social benefit ratio rose to 28.8 per cent. By 2003, however, following German unification, the integration of the East German population into the West German social system and the persistently high levels of unemployment engendered by unification, the ratio had reached a record high of 32.9 per cent. In the lengthy boom that lasted until the financial crisis, the social benefit ratio fell to under 30 per cent, but by 2009, in the wake of the financial crisis, it had risen again to the 2003 level.

The most important pillars of the German social model that developed in the post-war period up to unification are outlined below:

- The 1949 Collective Bargaining Act guaranteed the autonomy of the parties to collective bargaining in wage setting and the determination of many other labour standards.
- The 1951 Dismissal Protection Act, the 1969 Statutory Sick Pay Act and other items of labour legislation improved the protection afforded to employees.
- The 1951 Codetermination Act for the Coal, Iron and Steel Industries and the 1952 Works Constitution Act institutionalized codetermination at establishment and company level. The 1972 amendment to the Works Constitution Act and the 1976 Codetermination Act further extended employees' rights of codetermination.
- In 1957, the up-rateable pension was introduced; increases were made automatically in line with the general evolution of wages.
- Financial transfers to families were extended in 1954, when the Child Allowance Act came into force, and again in 1958 with the introduction of the income-splitting tax law for married couples.
- Active labour market policy was established in 1969 with the passing of the so-called Employment Promotion Act, which introduced systematic promotion of further vocational training for the unemployed.
- The goal, enshrined in the Constitution, of ensuring that all parts of the country enjoyed equivalent living conditions required that a system of fiscal equalization between the rich and poor *Länder* be put in place.

Even though the development of the welfare state did not follow a master plan but happened only through consensus, a number of overarching basic principles underpinning the German social model can be identified. The first, which became established with the 1957 pension reform, is the principle of safeguarding existing living standards, according to which the cash benefits paid in the event of unemployment, retirement and illness are linked to the previous level of earnings. The second is the principle that living conditions should be equivalent across the country. This was ensured not only by means of the fiscal equalization system but also through collective bargaining policy, which, despite the existence of regional bargaining in many industries, did not permit large regional wage differences to develop. The third and final principle is that of equal pay for equal work in the same establishment, which, well before the EU directives, determined the pay of vulnerable workers. However, in contrast to the Scandinavian countries, with their solidaristic wage policies, the equal pay principle was not applied across establishments, which meant large differences between industries. The fourth is the principle of subsidiarity, according to which the central state intervenes in certain areas only when subordinate social units, such as the individual, family or parties to collective bargaining, cannot help themselves. The fifth principle is the combination of public financing and private service provision, which is characteristic of health care, long-term care and many other social services in Germany.

### 3. THE HARTZ ACTS: A PARADIGM SHIFT IN LABOUR MARKET POLICY

With the Hartz Acts the labour market policy philosophy of investing in further training for the unemployed and not forcing them into low-wage work was abandoned. By making considerable reductions in the material support available to the unemployed and deregulating precarious forms of work, the legislative process gave rise to a new labour market policy paradigm that might be described as 'placement in work at any cost'.

In 2002 the Federal Government appointed an expert commission chaired by the then human resource director at Volkswagen AG, Peter Hartz. The key message proclaimed by the Hartz Commission was a radical simplification of the bureaucracy the unemployed had to deal with. Jobcentres were to be created that would be one-stop shops and considerably improve the job placement service. After the vote in parliament, with the conservative majority in the lower house, nothing remained of this idea. The unexpected result was that, in the end, instead of the former two administrative regimes responsible for three different support payments, there are now three administrative regimes with two support payments.

The former income-related unemployment assistance for long-term unemployed was abolished and merged with social assistance to form the new unemployment benefit II, a basic subsistence benefit that was no longer income-related. This marked a break with the principle of maintaining living standards. Unemployed individuals with no entitlement to unemployment benefit I or whose entitlement had been exhausted were all treated the same, regardless of whether they had been in gainful employment for many years. Besides the abolition of unemployment assistance, there were also significant reductions in the level of material support, particularly in the case of unemployment benefit I. The maximum length of entitlement to unemployment benefit, which was 12 months but for older workers over 50 between 14 and 32 months, depending on age, was reduced to between 15 and 18 months for the over-50s. In addition, the long-term unemployed now have to accept any job offer paying up to 30 per cent of the customary local wage.

Table 1. Administrative regime and support measures for the unemployed before 2003 and in 2013, Germany

| Administrative regime |   | Support measures   |   |
|-----------------------|---|--|---|
|                       |   | Passive measures   | Active measures   |
| Before 2003           | Federal Employment Service                                | Unemployment benefit (63-68 per cent of former net income)<br>Unemployment assistance (53-58 per cent of former net income, income-tested) | Active measures for all registered unemployed   |
|                       | Local authority social welfare departments                | Social assistance (means-tested)   | Special support measures (drug counselling and so on in some cases employment measures as well) |
| 2013                  | Federal Employment Agency                                 | Unemployment benefit I (63-68 per cent of former net income)   | Active measures for unemployed on Unemployment Benefit I  |
|                       | Local authorities with sole administrative responsibility | Unemployment benefit II (social assistance means-tested)   | Active measures for unemployed on Unemployment Benefit II                                       |

Source: Author's compilation.

Other key measures were the deregulation of temporary agency work and so-called mini-jobs. In the case of temporary agency work, the time limit on the loaning of workers to any one company was abolished and derogations from the equal pay rule were permitted in collective agreements. Up to a certain earnings threshold, mini-jobs are exempt from income tax and social insurance contributions. The consequence of this is that married individuals employed in mini-jobs continue to benefit from health insurance at no cost via their spouses and also retain all the tax reliefs granted under the splitting arrangements.

The most important results of the evaluations of the Hartz Acts can be summarized as follows:

- The two deregulated employment forms – temporary agency work and mini-jobs – have gained considerably in importance. The number of temporary agency workers rose from 300,000 in 2003 to around 900,000 in 2013, while over the same period the number of people employed in mini-jobs rose from around 5.5 million to 7.5 million.
- The expansion of the low-wage sector and of mini-jobs offering only limited hours has led to an increase in the number of workers who top up their low incomes with unemployment benefit II. As a result, in 2011 almost one-third of total expenditure on unemployment benefit II – some 10.7 billion euros a year – went to households with at least one economically active member.



– The evaluations have not produced any unambiguous findings on the core element of the Hartz philosophy, namely improvement of the job placement service. Consequently, to this day we still do not know whether the core objective of the Hartz Acts – improvement of the job placement services – has been achieved. However, fear of a descent into the transfer system has increased among the unemployed and increased their readiness to make concessions. Firms are now able to fill poorly paid positions more easily (Kettner, Rebien, 2007).

The most contentious effects of the Hartz Acts are those on employment levels. Horn and Herzog-Stein (2012) have compared the employment intensity of three economic cycles (first quarter of 1999–first quarter of 2001; second quarter of 2005–first quarter of 2008; and second quarter of 2009 until the current end point). In the first upturn, employment intensity – in other words, the percentage increase in the level of gainful employment when GDP rises by 1 per cent – was 0.43 per cent and in the two subsequent upturns it was just 0.35 per cent and 0.39 per cent, respectively. Thus the employment dynamic tended to weaken after the Hartz Acts. The two upturns after they came into force were almost wholly driven by exports. The Hartz Acts enabled the country, even in the strong upturn of 2005–2008, to continue its policy of internal devaluation within the euro zone by means of below-average wage increases and unit wage costs relative to other euro-zone countries (Stein, Stephan, Zwiener, 2012). Because domestic demand and, consequently, imports as well did not keep pace with the growth in exports, trade imbalances within the euro zone increased, which is one of the principal reasons for the euro-crisis. Thus the impact of the Hartz laws has a European dimension.

#### 4. EROSION OF THE COLLECTIVE BARGAINING SYSTEM, LOW WAGES AND MINIMUM WAGES

##### 4.1. *Expansion of Low-Wage Sector*

Since the end of the 1990s, German wages have risen less than those in the rest of the EU. One principal reason for this is the rapid expansion of the low-wage sector, which was under way before the Hartz laws. The share of low-wage workers rose from 18.8 per cent in 1995 to 23.8 per cent of all workers in 2011. One particularity of the German low-wage sector is its marked downward dispersion, because there is no effective lower limit to prevent very low wages. In 2011, 6.1 million workers were paid less than the minimum wage of 8.50 euros demanded by the German Trade Union Federation, while 2.9 million in fact earned less than 6.00 euros per hour (Kalina, Weinkopf, 2013).

The expansion of the low-wage sector began around 10 years before the Hartz Acts. The causes were changes in the behaviour of employers (who took advantage of high unemployment to quit employers' associations and cease to be bound by collective agreements), and the opening up of many previously public services (post, railways, local transport and so on) to private providers who were not bound by collective agreements and competed with state-owned companies by engaging in wage dumping. The Hartz Acts did not set this process in motion but, as already noted, prevented low-wage work from being reduced in the strong upturn from 2005 onwards. The most important influence in this regard was exerted by the two employment forms deregulated in the Hartz Acts (see Section above), which are overwhelmingly badly paid. Among employees in mini-jobs, the share of low-wage workers was 71 per cent in 2011 (Kalina, Weinkopf, 2013) and around two-thirds for temporary agency workers.

#### *4.2. The Bumpy Road to a National Minimum Wage*

Coverage by collective agreement, which was around 80 per cent prior to 1990, had declined to 60 per cent in western Germany and to 48 per cent in eastern Germany by 2012. In many small and medium-sized enterprises and service industries, wages are determined unilaterally by firms, because collective agreements are not in force and works councils have not been set up. As a result, the trade unions as well as the Social Democratic Party and the Greens have reconsidered their rejection of state intervention in the wage-setting process and have been campaigning for the introduction of a national minimum wage. The first grand coalition (2005-2009) extended the possibilities to negotiate industry minimum wages. In 2013 minimum wages were agreed with employers' associations in 12 industries and have been declared generally binding by the Federal Government. The effects of minimum wages on pay levels and employment have been investigated in eight industries, in some cases using a difference in differences estimation. No negative employment effects were observed (Bosch, Weinkopf, 2012).

In December 2013, the SPD had made its participation in the grand coalition dependent on the introduction of a national minimum wage, which is now to take place at the beginning of 2015. The draft of the new law from March 2014 only provides the exemption of apprentices, young workers under 18 years and long term unemployed (more than one year unemployed) for the first 6 months of their employment. The around 1.5 million apprentices are by far the biggest group which is exempted. They receive so called "training allowances" which are agreed by the social partners in collective agreements. Until the end of 2016 the social partners should have the possibilities to deviate from the NMW by a collective agreement on industry minimum wages. This is meant to encourage collective bargaining in low wage industries. The draft also stipulates additional measures to strengthen collective bargaining. The possibility to negotiate higher industry minimum wages should be extended to all industries and the procedure to extend collective agreements should be facilitated by adding a "public interest in avoiding the distortion of competition" in the law. A "Commission of the Social Partners" should regularly reappraise the level of the NMW. The Commission should consist of nine members. Eight members are to be selected by the social partners (three delegates of the trade unions, and three of the employers association plus two academics also proposed by the social partners). The social partners should agree on an independent chairperson. The academics should do not have the right to vote. The Commission should decide on June 10, 2017 the first increase of the NMW in January 2018. Then, the NMW should be increased yearly according to the average of the increases of collectively agreed wages. The three year freeze of the NMW was part of the compromise between the political partners. Customs should be strengthened by increasing its staff.

#### 5. OLD-AGE INSURANCE

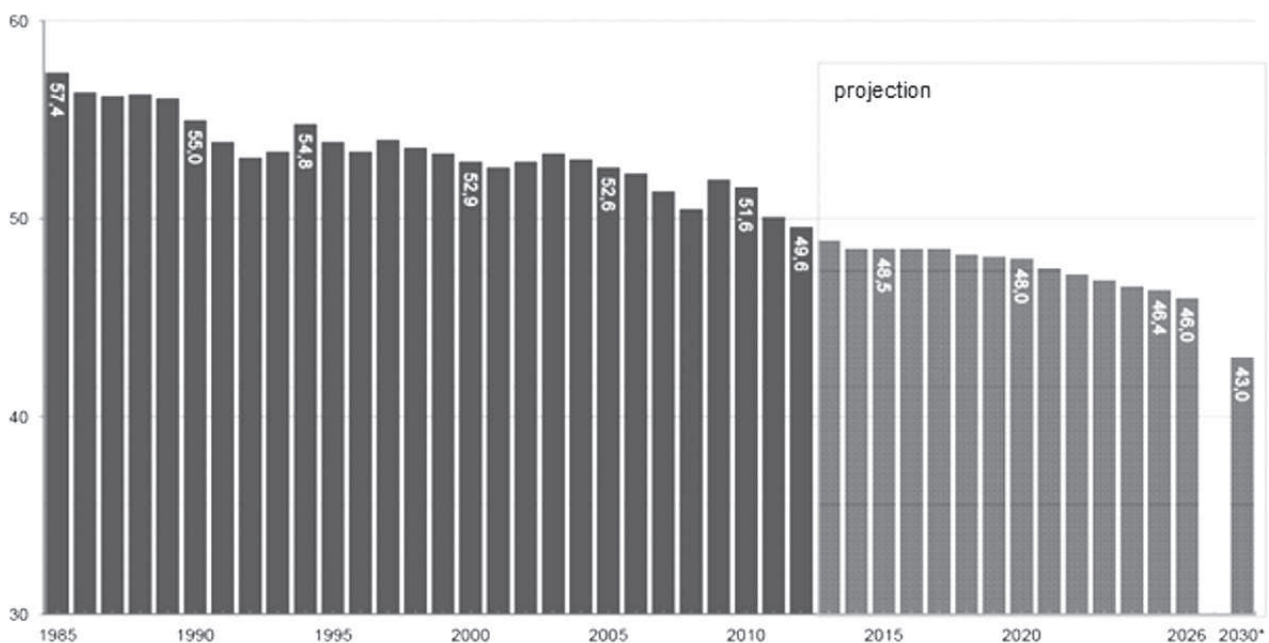
The vast majority of the economically active population is insured through the statutory old-age insurance scheme. The only groups exempt from the statutory scheme are career public servants (*Beamte*), whose pensions are funded directly from the federal government budget, and self-employed workers. Farmers and certain other groups have special funded occupational schemes. For the liberal professions with their own regulatory bodies (doctors, pharmacists, architects and so on), membership of a pension scheme organized

at the level of the individual federal state (Land) is compulsory. There are also company pension schemes, although these cover only a section of the labour force.

The level of individual pensions depends crucially on length of employment in insurable jobs and is not calculated on the basis of the absolute level of earned income and contributions paid but the relative level compared to average earnings over the entire working life. However, because benefits are also paid for certain periods without gainful employment and payment of contributions, the link with employment is supplemented by the solidarity principle. Credits are given especially for periods spent in vocational training and for time taken out of the labour market in order to raise a family or care for family members.

In order to tackle the major structural crises in manufacturing industry and in eastern Germany following German unification, several series of heavily subsidized labour market programmes were introduced that created various possibilities for bridging the period between exit from a firm and early retirement. As a result, the employment rate for 55-64 year olds, which was 51.9 per cent in 1970, fell to 36.8 per cent in 1991 and remained low until the end of the century (37.6 per cent in 2000). The high costs of early exit from work, combined with population ageing and longer time spent in retirement, led to a change of policy at the end of the 1990s. From 1997, the age limits were increased step by step. The earliest age at which a pension can be taken, with reductions, is 63. The retirement age for women was equalized with that for men by 2010. From 2012, the retirement age will be increased to 67 by 2029.

Figure 1. Evolution of net standard pension level before tax 1985 – 2026 and 2030 Level of the net standard pension before tax (45 contribution years) as % of average annual earnings



\* Lower limit of level safeguarding clause.

Source: IAO, Sozialpolitik Aktuell ([http://www.sozialpolitik-aktuell.de/tl\\_files/sozialpolitik-aktuell/\\_Politikfelder/Alter-Rente/Daten-sammlung/PDF-Dateien/abbVIII37.pdf](http://www.sozialpolitik-aktuell.de/tl_files/sozialpolitik-aktuell/_Politikfelder/Alter-Rente/Daten-sammlung/PDF-Dateien/abbVIII37.pdf))



Since 1992 the pension level has also been reduced several times. In 2005, the so-called ‘sustainability factor’ was introduced as a means of taking account, in determining pension increases, of the contributor/beneficiary ratio. When this ratio falls, so do pension increases. As a consequence the so-called ‘standard pension’ level of a pensioner with 45 contribution years and average earnings will decline further in the coming years. In 1985, for a standard pensioner it was 57.4 per cent of the average wage; by 2012 it had fallen to 49.6 per cent and will decline further to 43 per cent by 2030 (FIG. 1). The pension gap cannot be filled by the subsidized private “Riester-pension”, which was introduced in 2002 (named after the then Minister of Labour). The Riester pension is not obligatory and by 2011 only about 40 per cent of those entitled had entered into a Riester contract. Take-up rates are particularly low among poorly paid workers (Geyer, 2011, p. 19).

Because the German statutory pension insurance scheme is employment-dependent, at present, a worker just above the low-wage threshold (75 per cent of average earnings) has to work for 37 years full-time in order to accrue a pension entitlement above the basic social protection, known as social assistance for older people. By 2030, it will already be 45 years, which very few low earners actually achieve (Riedmüller, Willert, 2009). The pension level also falls after long periods of unemployment. The cumulative effects of the changes will lead to a drastic increase in the share of pensioners with an income below the level of basic social protection, particularly in eastern Germany.

## 6. FAMILY POLICY

The male single breadwinner model/housewife-carer model underwent a renaissance in the post-war period, because it helped to differentiate the German Federal Republic from the GDR. The dominance of this model means that family policy in Germany is even today characterized largely by transfers and tax relief, while services for children and families, particularly in the form of childcare and whole-day schools, play a significantly less important role than in the Scandinavian countries, for example (TAB. 2). Also striking is the high share of tax relief, which reflects the particular significance of status protection in family policy, because tax relief in progressive tax system favours families with higher incomes.

Table 2. Share in GDP of and distribution of expenditure on family policy, Germany, 2009 (%)

|                | Cash benefits | In-kind | Tax-relief | Total |
|----------------|---------------|---------|------------|-------|
| United Kingdom | 2.46          | 1.38    | 0.38       | 4.22  |
| France         | 1.44          | 1.76    | 0.78       | 3.98  |
| Sweden         | 1.58          | 2.17    | 0.00       | 3.75  |
| Denmark        | 1.63          | 2.27    | 0.00       | 3.90  |
| Germany        | 1.16          | 0.89    | 1.01       | 3.07  |
| Italy          | 0.78          | 0.80    | 0.00       | 1.58  |
| United States  | 0.11          | 0.59    | 0.52       | 1.22  |
| OECD average   | 1.41          | 0.94    | 0.28       | 2.61  |

Source: <http://www.oecd.org/els/soc/oecdfamilydatabase.htm>, Excel table.

German family policy privileges marriage through the income-splitting system for assessing married couples' tax liability and the derived social insurance entitlements for spouses. The combination of financial incentives for low levels of economic activity or even inactivity and the inadequate provision of childcare and half-day schooling has strongly influenced women's participation in the labour market. Between 2001 and 2012, the participation rate rose by 9 percentage points, from 58.7 per cent to 67.7 per cent, taking it well above the average for the EU27, in which the female participation rate in 2011 was 58.5 per cent. However, because the share part-time workers increased disproportionately at the same time, the participation rate in full-time equivalents rose by only 5.5 percentage points, from 46.5 per cent to 51.8 per cent, which is only slightly above the EU27 level of 49.9 per cent in 2011 (European Commission, 2013, pp. 403, 409).

Since the mid-1990s, growing dissatisfaction with the difficulties of reconciling paid work and family life, which is also increasingly influencing voting behaviour, has led to the gradual establishment of a modernized model of the family alongside the old one:

- 1996: entitlement to a half-day nursery place for children aged between four and six was enshrined in law;
- 2001: full-time employees in companies with more than 15 employees were given the right to reduce their working time and move to part-time employment;
- 2003: the Federal government made available 4 billion euros for the *Länder* to develop all-day schooling;
- as of August 2013, every child aged between one and three has a legal entitlement to a childcare place;
- 2007: following the Swedish model, 14 months' paid parental leave was introduced in addition to the existing statutory maternity leave. Between 65 and 100 per cent of the net monthly income is paid up to a maximum of 1,800 euros. Parents cannot claim the full 14 months unless the father takes at least two months' leave.

The take-up rate for the parental allowance (*Elterngeld*) is very high and the benefit has achieved its aims. Family incomes in a child's first year of life are increased by an average of 400 euros per month. The two months of paternal leave are taken by 25 per cent of fathers and the incentives to return to paid work have increased (Wrohlich *et al.*, 2012). In a child's first year – that is, during the period when the parental allowance is paid – the participation rate for mothers has declined but it rose again subsequently.

However, we cannot speak of an unambiguous change of direction in family policy. The old model has been reinforced by the childcare supplement for parents (the so-called *Betreuungsgeld*), which was introduced on 1 August 2013. Parents who do not send their 1 to 3 year olds to a nursery but look after them themselves receive a supplementary monthly allowance of 150 euros. Parents with low levels of education and low incomes tend to opt for the child care supplement, however, even though their children have a particular need for the support and stimulation nurseries offer (Wirth, Lichtenberger, 2012).

Thus, at great expense, German family policy supports two contradictory models of the family, which is not particularly effective. Mothers' working time is particularly negatively influenced by the income-splitting arrangement and the derived entitlement to health insurance without contributions, while public childcare, the advance on maintenance payments and the tax relief for childcare costs all have a positive influence in this regard (Prognos, 2012, p. 11).

## 7. LONG-TERM CARE INSURANCE

In the traditional German social model, it was difficult to justify the fact that the risks of accident and sickness were covered by insurance schemes, whereas long-term care, an equally universal risk, had to be funded privately. After a debate that had dragged on for 20 years or so statutory long-term care insurance came into force in 1995 (Bäcker *et al.*, 2010, pp. 181-98).

The long-term care insurance scheme was modelled on the health insurance system. Everyone insured in the statutory health insurance scheme and private health insurance is obliged to take out long-term care insurance as well. The benefits provided depend on the level of care needed. The contribution rate for the scheme was fixed in 1995 at 1 per cent of total gross wages, with contributions to be paid equally by employers and employees. Unlike the health insurance scheme, the long-term care insurance scheme is a partial coverage scheme. Its fixed-rate benefits cover only a part of the costs. Moreover, the level of benefits is specified and cannot be adjusted when costs rise by increasing contributions, as is possible in the health insurance system. This leads to real reductions in benefits, which have to be absorbed privately or by the social assistance system.

Because of this inherent tendency towards reduced benefits and, at the same time, increasing care needs, particularly for in-patient nursing care, the sustainability of the funding for long-term care insurance was a subject for debate. A mini-supplementary long-term insurance scheme that is both fully funded and private in line with the Riester model for top-up pensions was introduced in 2013.

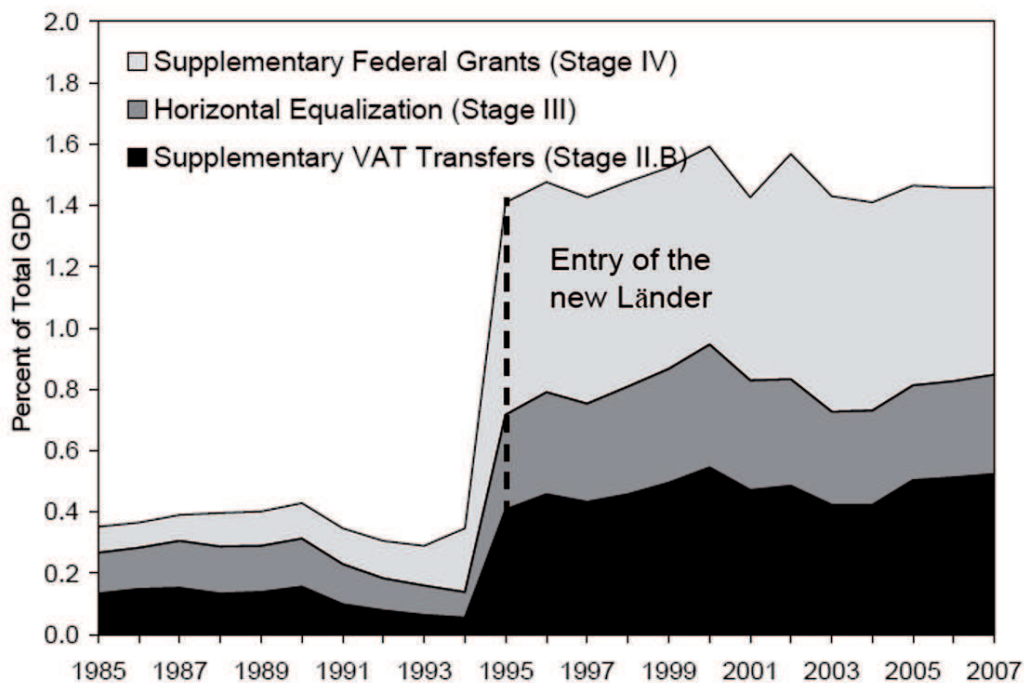
In the end, daily care rates were increased in 2008 and 2013. The contribution rate had already been raised to 1.7 per cent in 1996 and to 2.05 per cent in 2013. In 2005, the contribution for childless people aged between 23 and 60 was increased by 0.25 per cent, because the Federal Constitutional Court ordered that greater consideration be given to the expenditure of families with children, which as a rule are no longer taken into account. The number of insurance benefit recipients rose from 1.56 million in 1996 to 2.36 million in 2011. The majority of recipients are women (65 per cent in 2011). The scheme's income and expenditure are stable because benefits are capped. The aim of reducing local authority expenditure on social assistance has been achieved. Such expenditure fell between 1994 and 2001 from 9.06 to 2.9 billion euros (Bäcker *et al.*, 2010, p. 194), although it had risen again to 3.6 billion euros by 2011.

## 8. REGIONAL FISCAL EQUALIZATION

The regions of Germany differ considerably in their economic strength. Consequently, the goal of 'creating the same living conditions' in all parts of the country, which is enshrined in the German constitution, can be achieved only by equalising the differences in financial strength between the *Länder*. In contrast to many other countries, the *Länder* and the municipalities in the German federal system have little autonomy when it comes to revenue. Virtually all taxes are fixed at a uniform level across the country as a whole (Stehn, Fedelino, 2009, p. 6). However, a complex system of fiscal equalization ensures that revenues are largely evened out across the *Länder*. Those that have below-average financial strength are brought up to the national average, while the fiscal capacity of the donor *Länder* is reduced to that same average.

After reunification, which brought with it increasing wage inequality, fiscal equalization became increasingly important. In 1993, the five new East German *Länder* were incorporated into the fiscal equalization system and up to 1.5 per cent of GNP was redistributed among the regions (FIG. 2). In the Solidarity Pact, which runs from 2005 to 2019, central government is making available to the new *Länder* some 207 billion euros of additional investment funds, to be paid in diminishing instalments. The federal government's additional expenditure is funded by the so-called 'solidarity surcharge', a surtax on income, capital gains and corporation tax levied since 1998 at a rate of 5.5 per cent (7.5 per cent between 1995 and 1997).

Figure 2. Evolution of the equalization transfer system, Germany, 1985-2007



Source: Stehn, Fedelino (2009, p. 9).

Following reunification in 1991, wage levels in eastern Germany were around half those in western Germany. Wages had been even lower prior to reunification. If pension entitlements had been calculated on the basis of eastern German incomes, the differences in living conditions would have persisted for many decades. In order to prevent this, eastern German pension entitlements for each year of employment were multiplied by an uprating factor (the ratio of the average eastern German to the average western German income). However, because contributions are calculated on the basis of the lower gross incomes that still prevail in Eastern Germany, considerable transfers from West to East are required. In 2003 and 2005, the volume of redistribution attributable to unemployment insurance – at 7.8 and 6.3 billion euros, respectively – was close to the volume of transfers created by the fiscal equalization mechanism (6.8 and 6.9 billion euros, respectively). The volume of redistribution within the statutory old-age insurance scheme is even greater (BBSR, 2012, p. 188).



The regional fiscal equalisation system is now being heavily criticised because of its strong focus on the differences between eastern and western Germany and the inadequate funding of many local authorities in western Germany in particular. Federal legislation has placed many duties and responsibilities on the *Länder* and local authorities without making available the additional resources they require. This applies to assistance with living expenses (social assistance), the regulations on the funding of accommodation for recipients of unemployment benefit II, child and youth welfare, childcare and so on. The situation is exacerbated by the entrenchment of high levels of structural unemployment, which is increasingly affecting local authorities in western Germany. The consequences are increasing indebtedness in many local authorities and a drastic reduction in their ability to fund investment in material assets. Uniformity of living conditions is being increasingly undermined by this underinvestment in local infrastructure and reductions in services in many areas (for example, culture and education). Demands are being made for a complete reorganization of the regional fiscal equalization system. In particular, social benefits laid down in federal legislation should be financed by central government in order to reduce the burden on local authority budgets (Bertelsmann-Stiftung, 2012; Eichel, Fink, Tiemann, 2013).

#### 9. THE GERMAN 'JOBS MIRACLE' IN THE FINANCIAL CRISIS

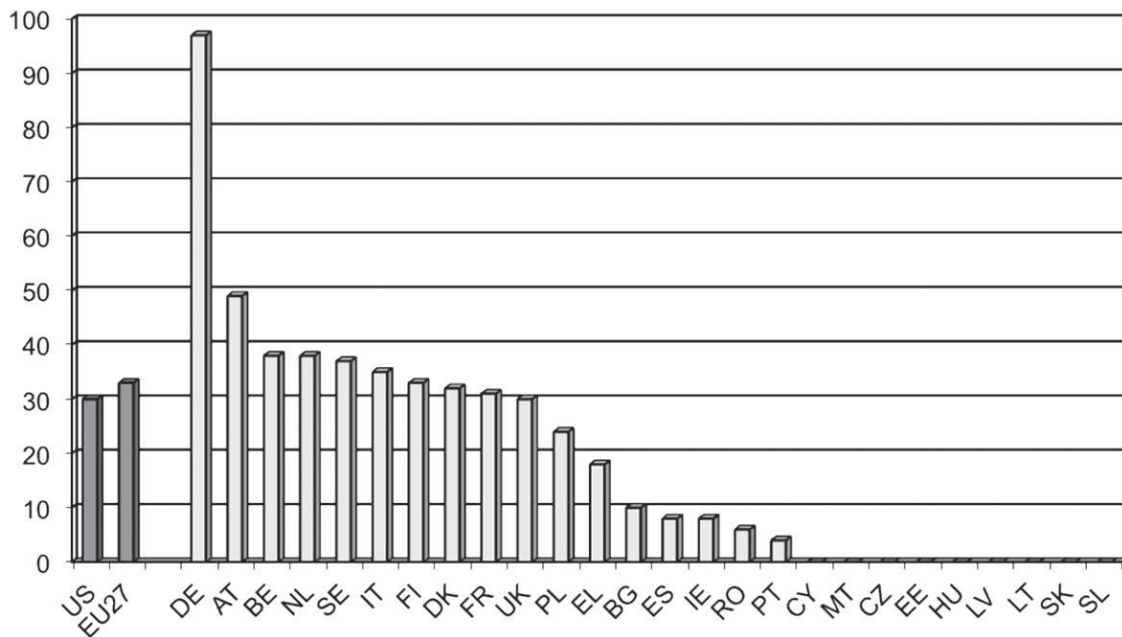
In the wake of the financial crisis, the German economy experienced its most severe slump since the Second World War (−4.9% of GDP in 2009). However, the effects on the labour market were different from those experienced in all other previous economic crises and in most other OECD countries. Employment did not decline as expected and unemployment did not rise. The Hartz Acts had created new sources of external flexibility; in the financial crisis, however, it was primarily internal flexibility that was strengthened. In order to achieve this, representatives of the federal government, the employers' associations and the trade unions agreed not only to avoid redundancies whenever possible but at the same time to maintain the number of new training contracts in the German dual vocational training system at the same level as the previous year in order to prevent an increase in youth unemployment.

Among the various labour market policy measures taken, short-time working played the major role. Before the recent financial crisis, short-time working was intended primarily as a buffer for short-term reductions in orders but not as a response to a deep, long-term crisis. The maximum period for claiming subsidies for short-time working was increased from 6 to 24 months. In addition a rich "tool box" of instrument to reduce working hours could be used. Almost half of German companies have introduced working-time accounts in recent years, the details of which are specified in most cases in an agreement with the works council (Groß, Schwarz, 2009). Furthermore, virtually all German collective agreements make provision for temporary reductions in standard working time in economic crises, usually without wage compensation, in order to avoid redundancies. In some industries, the social partners have agreed to give the actors at firm level opportunities to reduce the collectively agreed working time temporarily in order to avoid dismissals.

Almost all industrialised countries sought to ease the impact of the crisis to some extent by reducing working time. Some countries, such as France, Belgium, the Netherlands and Austria, have long-established, subsidised short-time working schemes, the conditions for

which were relaxed in the crisis. Only in Germany, however, was the reduction in labour input almost completely absorbed by a redistribution of work (FIG. 3).

Figure 3. Share of fall in total labour input due to fall in working hours per employee (2008-09)



Source: Eurostat (2010), <http://www.conference-board.org/economics/database.cfm>.

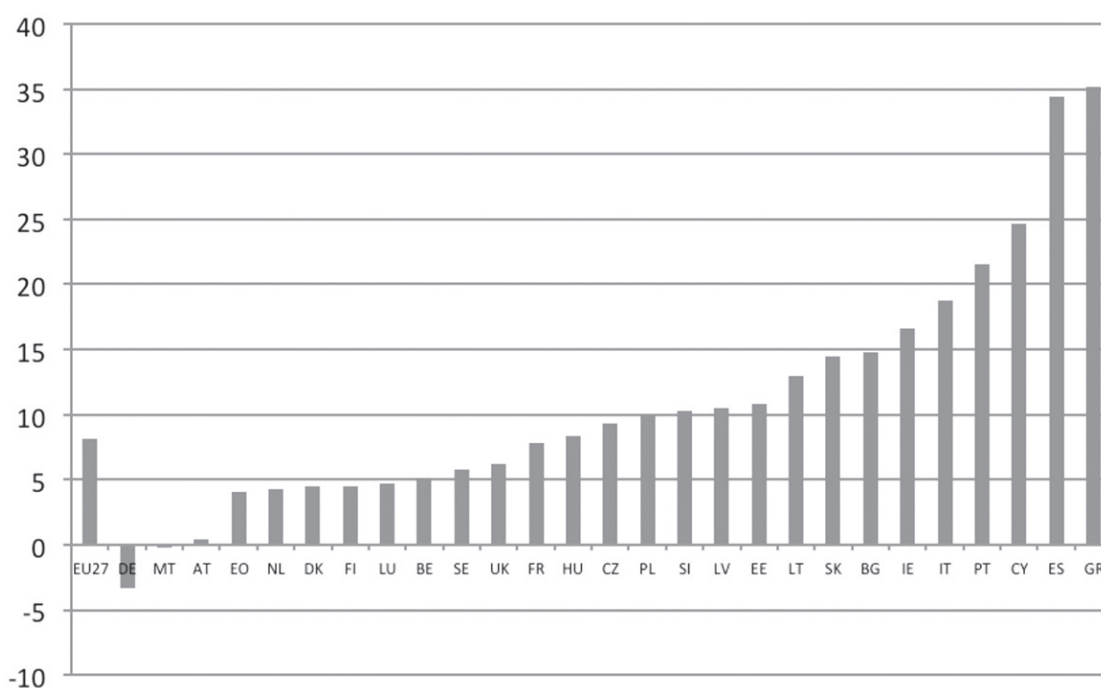
The second element of the German jobs miracle, which has been virtually ignored in the literature, was the prevention of high youth unemployment. Young people are a vulnerable group. In an economic recession they are often the group most hit by unemployment in the labour market since the first reaction of companies to a decline in orders is to stop recruitment. As outsiders leavers from the education and training systems they are not benefitting from employment protection.

Myriad studies have shown that occupational competencies acquired in apprenticeships systems with generally recognized standards make transitions into the labour market easier than competencies learned in school-based systems (Müller, Gangl, 2003). There was much concern that the success story of the dual apprenticeship system would come to an end in severe crisis in 2009 since it was difficult enough for companies to retain their workforce. In contrast to the development in most other European countries unemployment of young people did not rise very much and also not much faster than unemployment of workers in prime age (FIG. 4). In 2009 around 564,000 training contracts were concluded, 8.2% or 50,000 contracts less than in 2008. Because of the happy coincidence that the age cohort entering the labour market in 2009 also declined by around 50,000 the situation for young people looking for an apprenticeship did not deteriorate. In the following two years, the number of new trainees stabilised at about the 2009 level (BIBB, 2013, p. 10). In spite of economic difficulties most companies see a social obligation to train. In addition they

expect in the coming years because of shrinking cohorts of young people skill shortages and training is still seen as the most effective mechanism of recruitment.

Unions supported the integration of young people into the labour market. In 2009 and 2010 a second focal point in collective bargaining (beside avoiding dismissals) the recruitment of new apprentices and the continuation of employment after the completion of training. In the chemical industry, for example, the social partners agreed an annual quota of 9,000 new trainees for the period 2010-2013 and established a fund from which small and medium-sized firms in economic difficulty could be supported to provide training. In spring 2010 the social partners in the metal industry agreed to continue employment of all young journeymen for at least one year after apprenticeship (Bosch, 2011).

Figure 4. Increase in youth unemployment rates in percentage points in the EU (3/2008 – 3/2013)



Source: Eurostat.

## 10. CONCLUSION

In the past 20 years, the social security system has been further developed and reorganized at a rapid pace). The most important drivers of the changes are the ageing of the population, the increase in women's labour market participation and criticism of the traditional male single breadwinner model, German reunification and the emergence of new principles and approaches, in particular private provision, labour market deregulation and fiscal consolidation

The various, partially contradictory objectives led to a mix of policies in which progress and dismantling of the welfare state were closely juxtaposed. The erosion of the German

collective bargaining system and the deregulation of the labour market by the Hartz laws has far-reaching effects on the social welfare system. The reduction of pension levels over the coming decades will lead to an increase in old-age poverty because of the rapid expansion of the low-wage sector. At the same time, the increased expenditure needed to top up pay in the low-wage sector is a burden on the social budget. Combined with the expansion of the low-wage sector in Germany, this social policy has contributed to an increase in poverty and the shrinking of the middle class and has led to a more exclusive social model.

The integration of the eastern German population into the western German welfare state, and in particular the strengthening of the regional fiscal equalization system and uprating of the eastern German pension entitlements constitute a remarkable feat of solidarity. The introduction of long-term care insurance is also a major social policy reform that has strengthened social cohesion. The financial crisis saw successful mobilization of the strengths of the old German social model, which is based on social dialogue between the state and the social partners (short-time working schemes and vocational training also benefited from this). Through a combination of measures taken by central government and those agreed between the social partners, it was possible to avoid not only large-scale job losses but also an increase in youth unemployment. At the same time, the reform of the traditional German family model has begun with the development of child care and all-day schools and the introduction of the parental allowance, even though the old family model continues to be funded, which is both expensive and ineffective.

It is not clear in what direction the German model will develop. If the German jobs miracle turns out to have been a one-off event, the state and the employers' associations, captivated by the large-scale deregulation taking place in many European countries, may well return to the philosophy underlying the Hartz Acts, despite the success of internal flexibility in the crisis.

On the other hand, there is a growing realization that Germany's economic success depends not on a large low-wage sector but rather on an innovative manufacturing sector, a skilled workforce and a functioning system of social dialogue. The Hartz Acts have increased turnover in the labour market, it is true, but not employment levels. Moreover, the below-average increase in German wage costs (a form of social dumping) is one of the reasons for the imbalances in the euro zone.

Thus there are not only good social but also economic reasons for reinforcing the inclusivity of the German social model and at the same time adapting it to new needs.

The reforms needed to create a modernized but inclusive social model are fairly evident. The majority of the German population supports a statutory minimum wage and increased coverage by collective agreements. In view of the high level of local authority indebtedness, the regional fiscal equalization system will have to be reorganized. The traditional model of the family is losing support, making it possible to envisage a change of direction towards better reconciliation of paid work and family life, as well as increased investment in childcare and education. Old-age poverty can be avoided only by introducing compulsory supplementary pensions or slowing the decline in pension levels. With the grand coalition agreement of 2013, some steps in this direction seem to have been taken.

## REFERENCES

- BÄCKER G., NAEGELE G., BISPINCK R., HOFEMANN K., NEUBAUER J. (2010), *Sozialpolitik und soziale Lage in Deutschland*. Band 2: *Gesundheit, Familie, Alter und Soziale Dienste*. 5. Aufl. vs Verl. für Sozialwissenschaften, Wiesbaden.



- BBSR (BUNDESINSTITUT FÜR BAU-, STADT- UND RAUMFORSCHUNG) (2012), *Raumordnungsbericht 2011*, Bonn.
- BERTELSMANN-STIFTUNG (2012), *Neuordnung der föderalen Finanzverfassung Deutschlands ab 2020 - unter besonderer Berücksichtigung der Kommunen*, Gütersloh.
- BIBB (BUNDESINSTITUT FÜR BERUFLICHE BILDUNG) (2013), *VET Data Report Germany 2012, Fact and Analysis accompanying the Federal Report on Vocational Education and Training. Selected findings*, Berlin.
- BOSCH G. (2011), *The German Labour Market after the Financial Crisis: Miracle or just a Good Policy Mix?*, in D. Vaughan-Whitehead (ed.), *Work Inequalities in the Crisis? Evidence from Europe*, Edward Elgar, Cheltenham, pp. 243-77.
- BOSCH G., WEINKOPF C. (2012), *Wirkungen der Mindestlohnregelungen in acht Branchen*, Expertise im Auftrag der FES, Bonn.
- EICHEL H., FINK PH., TIEMANN H. (2013), *Vorschlag zur Neuordnung des Finanzausgleichs, Wiso-Direkt, Analysen und Konzepte zur Wirtschafts- und Sozialpolitik*, Friedrich-Ebert-Stiftung, Berlin.
- ESPING-ANDERSEN G. (1990), *Three Worlds of Welfare Capitalism*, Princeton University Press, Princeton.
- EUROPEAN COMMISSION (2013), *Employment and Social Developments in Europe 2012*, Luxemburg.
- GEYER J. (2011), *Riester-Rente: Rezept gegen Altersarmut?*, "DIW-Wochenbericht", 47.
- GROSS H., SCHWARZ M. (2009), *Arbeitszeitarrangements, Altersstrukturen und Corporate Social Responsibility in Deutschen Betrieben*, VS Verlag für Sozialwissenschaften, Wiesbaden.
- HORN G. A., HERZOG-STEIN A. (2012), *Erwerbstätigenrekord dank guter Konjunktur und hoher interner Flexibilität*, Wirtschaftsdienst, Heft 3, pp. 151-5.
- KALINA T., WEINKOPF C. (2013), *Niedriglohnbeschäftigung 2011. Weiterhin arbeitet fast ein Viertel der Beschäftigten in Deutschland für einen Niedriglohn*, "IAQ-Report", 2013-01.
- KETTNER A., REBIEN M. (2007), *Hartz-IV-Reform: Impulse für den Arbeitsmarkt*, "IAB-Kurzbericht", 19, Nürnberg.
- MÜLLER W., GANGL M. (eds.) (2003), *Transitions from Education to Work in Europe. The Integration of Youth into EU Labour Markets*, Oxford University Press, Oxford.
- PROGNOS AG (2012), *Wissenschaftliches Symposium zur Gesamtevaluation ebe- und familienbezogener Leistungen Berlin*, 28 June 2012, in [http://www.sozialpolitik-aktuell.de/tl\\_files/sozialpolitik-aktuell/\\_Politikfelder/Familienpolitik/Dokumente/gesamtevaluation.pdf](http://www.sozialpolitik-aktuell.de/tl_files/sozialpolitik-aktuell/_Politikfelder/Familienpolitik/Dokumente/gesamtevaluation.pdf) (accessed 30 July 2013).
- RIEDMÜLLER B., WILLERT M. (2009), *Aktuelle Vorschläge für eine Mindestsicherung im Alter*, Gutachten im Auftrag der Hans-Böckler-Stiftung 2009, Düsseldorf.
- STEHN S. J., FEDELINO A. (2009), *Fiscal Incentive Effects of the German Equalization System International Monetary Fund*, WP/09/124.
- STEIN U., STEPHAN S., ZWIENER R. (2012), *Zu schwache deutsche Arbeitskostenentwicklung belastet Europäische Währungsunion und soziale Sicherung, Arbeits- und Lohnstückkosten in 2011 und im 1. Halbjahr 2012*, "IMK Report", 77, November.
- TEPPE K. (1977), *Zur Sozialpolitik des Dritten Reiches am Beispiel der Sozialversicherung*, "Archiv für Sozialgeschichte", 17.
- WIRTH H., LICHTENBERGER V. (2012), *Form der Kinderbetreuung stark sozial selektiv – Ein europäischer Vergleich der Betreuung von unter 3-jährigen Kindern*, "Informationsdienst Soziale Indikatoren (ISI)", 48, Juli.
- WROHLICH K. et al. (2012), *Elterngeld Monitor*, "DIW Politikberatung kompakt", 61, February.

