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Employment Regulation and Labor Market Policy in Germany, 1991-2005

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ABSTRACT

Employment Regulation and Labor Market Policy in Germany, 1991-2005^{*}

The paper provides an overview of institutional provisions and reforms regarding employment protection, active and passive labor market policies in Germany as well as of actors' responsibilities in these areas. It covers the period between the early 1990s and the most recent Hartz reforms. Empirical data on labor market outcomes with respect to the levels and structures of both employment and unemployment complements this study.

JEL Classification: J60, J68

Keywords: employment protection, active labor market policy, unemployment insurance, Germany

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1 INTRODUCTION

1.1 Protection against Labor Market Risks in Germany

High unemployment is seen to be a central problem of post-unification Germany; this has often been linked to the high level of employment protection, the high labor costs and a strictly regulated labor market. Indeed, the German system of protection against employment risks is characterized by a high level of statutory employment protection for regular contracts, and the predominance of compulsory social insurance providing earnings-related benefits in case of unemployment after a sufficient contribution period. An earnings-related assistance benefit prolonging insurance-like status protection in case of long-term unemployment was replaced by a means-tested scheme in 2005, which also integrated the employable social assistant claimants under the local scheme. Thus replacing earnings-related long-term unemployment assistance with a means-tested flat-rate benefit was a major break with Germany's long tradition of status maintenance in case of unemployment. It was part of a broader policy shift towards activation also involving an overhaul of active labor market policies and organizational reforms in the labor market administration. Regarding employment protection, most reforms only addressed some liberalization at the margin of the labor market.

In terms of governance, social security, labor market policies and employment protection are mainly based on national legislation. Although there is no "market" for unemployment insurance and employment protection, market mechanisms have grown with regard to the governance and the service provision in active labor market policies in recent years. While the social partners had a formal role in the tripartite self-administration of the Federal Employment Office (BA) and a more limited role since the recent organizational transformation into the Federal Employment Agency (*Bundesagentur für Arbeit*), the social partners play only a minor role in supplementing national legal provisions through collective regulation. One can plausibly argue that the German system is more legislation-driven and more universal than the Dutch one in the sense that sectoral schemes and differentiations are much less important. This holds for all features except for

- (1) sectoral collective agreements with respect to dismissal protection,
- (2) enterprise-level agreements on employment stabilization in difficult economic situations (in exchange for flexibility in wages and working time), and
- (3) "social plans" in case of mass redundancies due to major business restructuring or plant closures (provision of severance pay and active labor market policies for dismissed workers).

Apart from sectoral and enterprise-level bargaining, the role of the social partners is limited, particularly since the recent reforms recommended by the Commission led by Peter Hartz in 2002. The social partners' influence on the governance of active labor market policy and the allocation of funds was previously considerable but significantly reduced by these recent "Hartz" reforms. Tra-

ditional German corporatism is still strong, but declining at the sectoral level with micro-corporatism at the firm level becoming stronger at the same time. This can be explained by declining membership in unions and employer associations and a weakening of collective bargaining coverage, i.e., the increase of opening clauses in sectoral agreements which also leaves more room for firm-level bargaining.

1.2 Protection Mechanisms and the Labor Market

Since the rise of mass unemployment following the first oil shock in the mid-1970s (see Figure 1), Germany tended use passive unemployment benefits and even active labor market policies in order to take labor out of the market, particularly those covered by relatively strict employment protection (e.g. through early retirement), and “hide” open unemployment through alternative benefits and active labor market measures (Manow/Seils 2000). Until recently, German active labor market policies had no clear priority on reintegrating the inactive people into the labor market and were not evaluated systematically. Access to unemployment insurance benefits and certain active labor market policy measures are tied to previous “normal” employment (*Normalarbeitsverhältnis*). Until recent reforms over the last ten years, passive unemployment benefits helped stabilize previous earnings even for the long-term unemployed, provided for an occupational safeguard clause regarding job suitability and facilitated bridges to early retirement. This passive use of labor market policies was also an indirect outcome of social partner involvement in the allocation of funds. Social partners favored externalization strategies, i.e. use of passive and active labor market policies to reduce labor supply, mainly in order to provide a bridge to early retirement (Rosenow/Naschold 1994, Ebbinghaus 2006). Hence, the German system provided thus far ample protection against labor market risks for labor market insiders: strong employment protection, quite generous unemployment benefits, and access to active labor market policies. This employment-centered and status-maintaining protection helped stabilize the German model of production tailored to a high-skill/high-wage equilibrium with long-term employment relations in the past (Estevez-Abe/Iversen/Soskice 2001, Streeck 1997). But the most recent changes towards less externalization and more activation undermine the old regime (Streeck/Trampusch 2005, Eichhorst/Kaiser 2006).

The German protection against labor market risks not only contributes to persistent problems regarding employment creation and the reintegration of long-term unemployed and inactive persons, but it also favors further labor market segmentation making the situation of more vulnerable groups less stable. Germany’s labor market institutions foster a *dual* labor market with high security and stability at the core and higher turnover and instability at the margin. In order to enhance labor market flexibility without threatening the stability of regular employment, gradual reforms fostered atypical employment. Thus the increasing numbers of temporary work agencies and fixed-term contracts but also of part-time workers and marginal employees (mini-job holders) go together with persistent long-term unemployment, slow increase in the labor force participation of

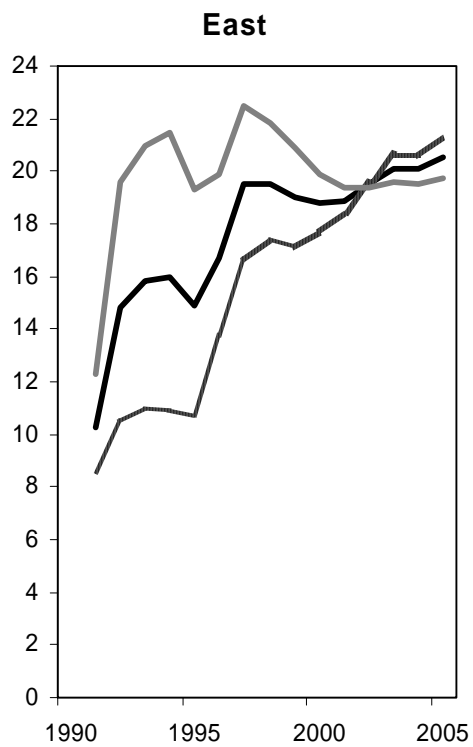
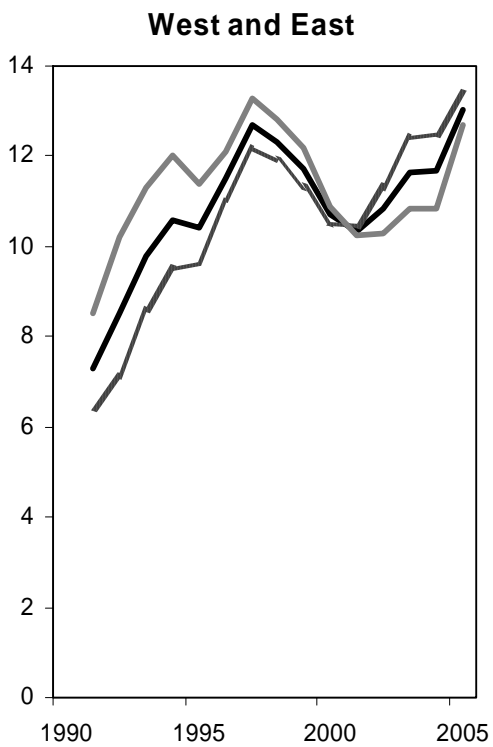
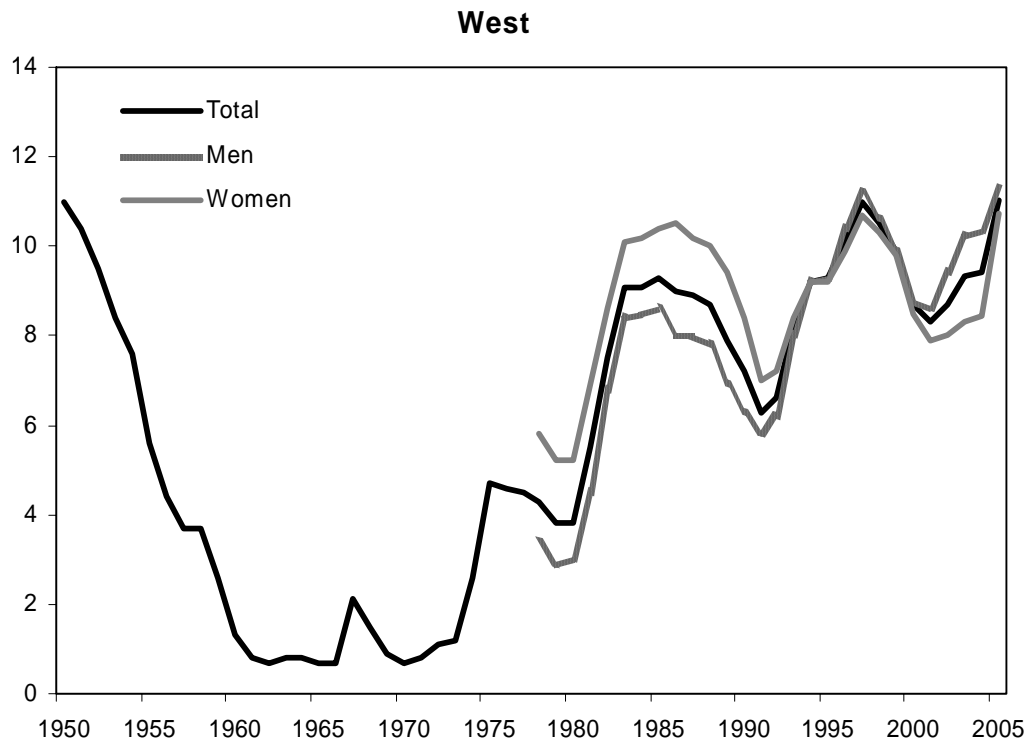
women, and low employment levels of older workers. Hence, German labor market institutions favor a certain segmentation of the labor market, maintaining security at the core and slowly increasing flexibility at the margin.

1.3 The Political Economy of Reforms

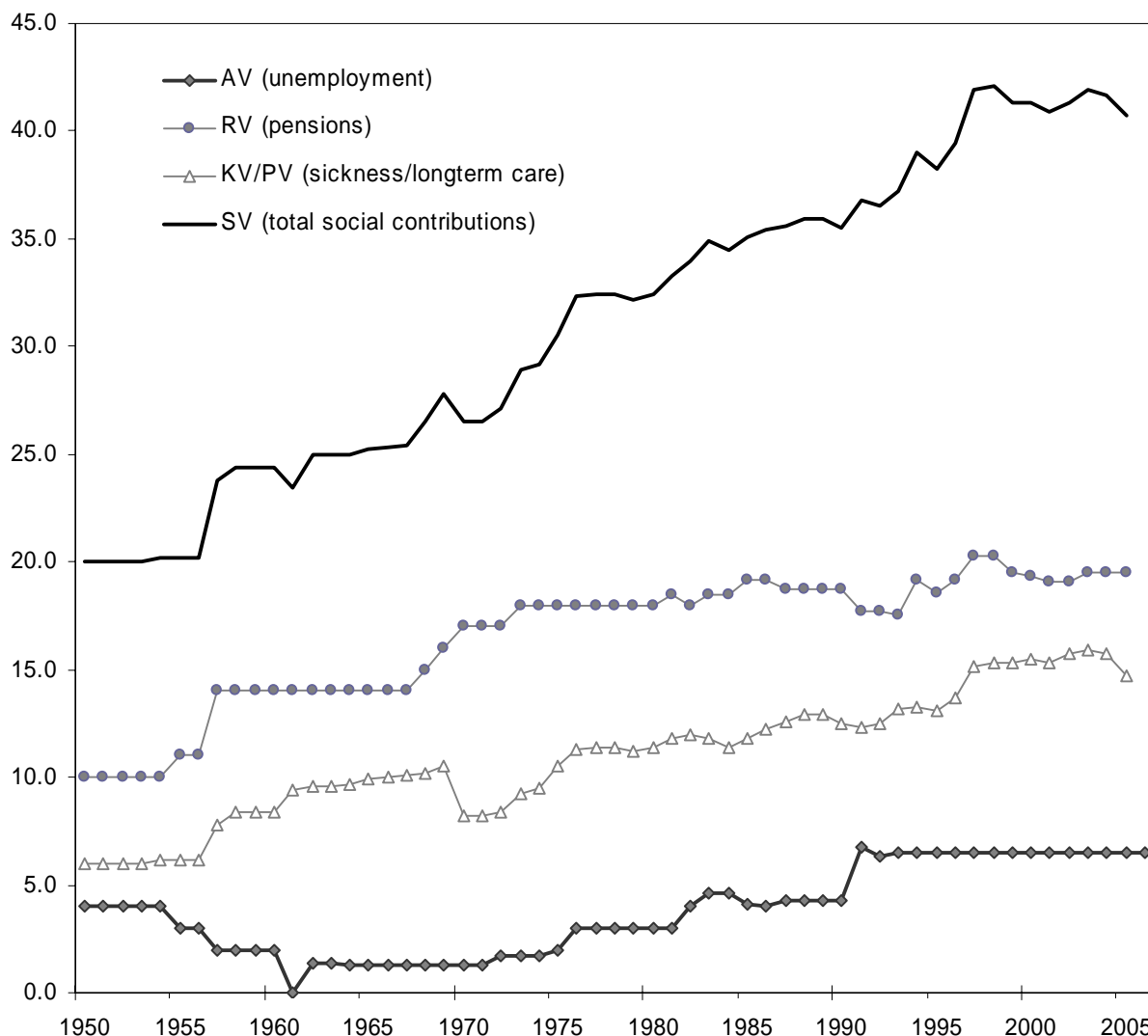
The increase of mass unemployment was already a phenomenon of the 1970s and 1980s, but German unification in 1990 made the problem more pressing. The integration of the post-socialist East German economy led to an increase in unemployment as overstaffed state firms were privatized and less new employment opportunities were created by German and foreign investment than had been expected during the first boom years. The political decision to finance a large share of the transition costs of East Germany through social insurance contributions (largely from the West) and not by general taxation increased the burden on labor costs, driving even more labor out of work. Policy makers in Germany tend to react to these problems in a selective way. The increase in social insurance contributions over the 1990s (see Figure 2), amplified by the “passive” approach to the unemployment problems after reunification, meant higher non-wage labor costs (Scharpf 2000, Manow/Seils 2000) that put pressure on the *Normalarbeitsverhältnis* and dampened new employment opportunities. At the same time, the growth of flexible jobs was facilitated by several legislative steps that required less employment regulation, lower or no non-wage labor costs, or even offered subsidies for such employment forms. A deregulatory reform of the core employment relations was seen as politically unfeasible, given the political consensus tradition and the unions’ defenders of these insider groups.

Due to the limited capacity of the federal government to act and the lack of tripartite arrangements, there is no strategic coordination of reforms in these areas that could mobilize policy complementarities in order to further employment growth and narrow the gap between standard and non-standard forms of employment. Neither the tripartite talks of the Alliance for Jobs that occurred during the mid-1990s under the Kohl government, nor the talks under the first Schröder government led to a consensus between the government and social partners on a reform of labor market policies. Therefore, Germany lacked a negotiated recalibration of social security and labor market flexibilization (or “flexicurity”) strategy that entails more flexible employment regulation in the core of the labor market, some re-regulation of the flexible segment and effective integration-oriented labor market policies. Although the Danish and the Dutch “flexicurity” arrangements attracted considerable public attention, they did not become part of a wider policy consensus between parties and social partners in Germany.

Figure 1: Unemployment rate (%) in (West) Germany 1950-2005



Source: BA, Federal Statistical Office; unemployed in % of dependent labor force.

Figure 2: Social contributions by employers and employees (% of gross wages)

Corporatism at a national centralized level was never as prominent as in the Netherlands – and attempts at establishing national tripartite talks in the late 1990s did not succeed. Substantial labor market reforms since the 1990s were mainly initiated by the federal government (see, e.g., the Hartz package or Schröder’s Agenda 2010) with the social partners being restricted to lobbying political actors (Streeck/Hassel 2003; Streeck/Trampusch 2005; Eichhorst/Kaiser 2006; Dyson 2005). There is no systematic coordination across policy areas via tripartite concertation as the “Alliance for Jobs, Vocational Training and Competitiveness”, created in 1998, was effectively deadlocked and could neither agree on reforms of labor market policies (except for the moderate JobAqtiv Act for young job-seekers) nor on flexibilizing employment regulation. The joint administration of active and passive labor market policies by the Federal Employment Office (BA) contributed to the externalization strategy of the past using passive policies to reduce labor supply. Theoretically, the joint responsibility in one agency could also facilitate an effective implementation of activation strategies by making passive benefits more contingent. However, there is no explicit link between

labor market policies and employment protection beyond the “social buffering” of mass redundancies through early retirement and other social plan measures. Although the Federal Ministry of Labor and Social Affairs is the major interface for policy design in labor market policies and employment protection, there is considerable intra-ministerial fragmentation between responsible departments, hampering coordinated policies. Moreover, given the importance of entitlement-based passive benefits and the limited state subsidies on top of insurance contributions, the resources available for active labor market policies are limited and may be squeezed out in times of high unemployment when they are need most.

The recent Hartz reforms, initiated by the Red-Green government after its re-election in 2002, aimed at both activating the unemployed (and social assistance claimants) and strengthening the reintegration capacities of active labor market policies as well as strengthening the job-creation potential of the economy through a partial deregulation of the labor market. The increase in labor supply (due to activation) was to be absorbed by a more flexible labor market, i.e. in “new” flexible segments such as start-ups, part-time and minor jobs, but also temporary agency work. While the shift towards activation means a break with the past, further steps in partial flexibilization fit in with the long-standing path of gradual reforms at the margin. Nevertheless, the Hartz reforms are a reform package addressing passive and active labor market policies, employment protection, and an organizational reform of both the employment office and communal responsibility. Overall, however, in contrast to the Dutch experience of rather “experimental” changes in labor market policies and quite substantial governance reforms, German employment protection, unemployment insurance and active labor market policy still show considerable continuity and stability – despite intense public debates and the Hartz reforms that are seen as a fundamental break. Given the growing role of flexible employment contracts, the so far institutionally stabilized core of the labor market comes under increasing pressure.

Table 1: Major reforms 1990-2006

	Active labor market policies	Passive labor market policies	Employment protection
1993			Unified notice period for blue-collar and white-collar workers
1994	Allowing private job placement agencies besides the public BA	Marginal cut of unemployment insurance benefit and unemployment assistance, stricter sanctions, but prolongation of favorable treatment of older unemployed	Extension of act on temporary employment
1996		Revision of old-age part-time employment law (used for early retirement)	Lifting of size threshold for dismissal protection; stricter social selection criteria; and liberalization of temporary contracts
1997	Reform of active labor market policy schemes (training, wage subsidies)		
1998	New Third Book of the Social Security Act	Tighter sanctioning, availability and eligibility criteria for unemployment insurance benefits, e.g. longer employment record required	
1999		Easing of availability criteria in unemployment insurance	Lowering of threshold for dismissal protection, reestablishment of broad social selection criteria;
2000	Better cooperation between PES and municipalities	Expansion of old-age part-time work	
2001			Additional restrictions on renewal of temporary contracts, but more flexibility in fixed-term employment of older workers
2002	Moderate steps towards activation (JobAktiv), introduction of profiling; placement vouchers and liberalization of private placement agencies	Moderately stricter sanctioning criteria (JobAktiv), stricter means-testing in unemployment assistance	
2003	Hartz I and II: introduction of training vouchers; new measures promoting employment of older workers; new start-up grant (Me Inc.)	Hartz I and II: requirement of early registration with PES in case of unemployment; stricter sanctioning, mobility requirements	Broader definition of marginal jobs; lower age threshold (52) for fixed-term employment without reason
2004	Hartz III: reorganization of public employment service with stronger emphasis on effectiveness and cost efficiency, reduced role for social partners, stronger element of quasi-	Duration of unemployment insurance benefit for older workers reduced from 32 to 18 months (effective only in 2006); additional sanctioning reasons	Higher threshold for dismissal protection, narrow selection criteria; formal option of severance pay; far-reaching liberalization of temporary agency work, but in exchange for equal treatment or

	Active labor market policies	Passive labor market policies	Employment protection
	markets/private service providers; integration of unemployment insurance benefit and benefits during training; reform of direct job creation schemes		first time collective agreements
2005	Hartz IV: new governance for activation of long-term unemployed; flexible institutional repertoire including public employment opportunities	Hartz IV: replacement of earnings-related with flat-rate unemployment assistance with emphasis on activation, i.e. stricter availability criteria	
2006		Stricter activation provisions through Hartz IV amendments; prolongation of longer unemployment benefits for older workers	

Source: authors' compilation; see Tables 2 and 12 for more details.

2 EMPLOYMENT PROTECTION IN GERMANY

2.1 General and Historical Development

Germany's far reaching employment regulation is based on different sources resulting in a high degree of legal complexity and juridification ("Verrechtlichung") by specialized employment legislation (and social policy rules), by court-based law-making (Labor Courts and Social Courts), and collective agreements at sector or regional level as well as firm-based agreements with works councils. Legally, there is a fundamental difference between permanent "normal" and fixed-term (temporary) contracts and other forms of "atypical" employment, the former guaranteeing substantial employment protection as well as social security coverage and the latter providing some form of flexibility to employers in terms of employment protection and lower or no social contributions, though the use of fixed-term contracts is also regulated. There is no differentiation in employment protection (and social contributions) with respect to working time above the "mini-job" earnings limit. Yet there are additional forms of flexible employment such as temporary agency work, "mini-jobs", and self-employed work, that provide some additional flexibilization in the labor market.

The history of employment protection in Germany is characterized by a high level of stability in dismissal protection for regular contracts with most reforms only addressing the firm size threshold (lifted from five to ten employees in 1996, lowered to five in 1999 and lifted again to ten in 2004) and the range of social selection criteria in case of dismissals for business reasons. However, although there is a clear long-term trend towards greater flexibility at the margin, there have also been some attempts at more restrictive approaches towards "atypical" employment, some of which were revoked shortly after. Most prominent are more liberal options regarding renewal and

maximum duration of fixed-term contracts in 1997 (but some tightening regarding fixed-term contracts without valid reason in 2000), a lowering of the upper age limit for unrestricted access to temporary contracts in 2000 and 2003 as well as a stepwise liberalization of temporary agency work over the last decade, complemented by the introduction of “equal treatment” and collective agreements.

2.2 Permanent Contracts

Dismissal protection of permanent (open-ended) contracts sets in after a probationary period of six months during which only minimum requirements and a short notice period of two weeks apply. Although longer or shorter probationary periods can be agreed upon by individual or collective agreements, statutory dismissal protection will set in after six months in any case. However, legal dismissal protection does not apply to small firms with less than 10 employees (about 6.5 million employees or 24%) or, prior to 2004: 5 employees (3.5 million employees or 13% of all the gainfully employed). With respect to permanent contracts, individual dismissals by the employer are possible if certain conditions are met (minimum provisions based on legislation, supplemented by collective agreements or individual contracts).

The legal minimum notice period is four weeks for both employer and employee (except for small firms with less than 10 employees that are exempt from statutory dismissal protection). Minimum notice periods for employers increase with tenure, e.g. 2 months after 5 years of service, 4 months after 10 years of service, 6 months after 15 years of service. Longer notice periods can be introduced through collective agreements or individual contracts, shorter notice periods only through collective agreements. There is no legal obligation to severance pay (only an option under mass dismissal rules). In case of disputes it is decided according to rules of thumb derived from court-based law (50% of last monthly salary times the number of years of tenure). Additional regulation is provided by collective agreements, particularly for older workers in case of dismissal (facilitating a bridge toward early retirement). Recent collective agreements (2004) stipulate severance pay after 25 years of service, for example, the chemical industry pays 6 months' worth of salary from age 60 onwards, the metal industry agreement provides for 9 months from age 59 onwards, and the public sector (West) and postal service even pay for 18 months from age 55 onwards. Severance pay is increasingly taxed and is now partly taken into calculation of means-tested unemployment benefits.

Table 2: Dismissal regulation

Procedural aspects:
<ul style="list-style-type: none">▪ written dismissal statement;▪ notice periods (§ 622 BGB): the normal notice period for employees is four weeks; the notice period for employers increases with job tenure to up to seven months after 20 years of service; these legal minimum notice periods can be extended in individual contracts or through collective agreements (shortening is only possible through collective agreements);▪ specific notice period of two weeks in case of immediate dismissal;▪ consultation of works council required (§ 102 BetrVG);
Valid reasons for dismissal as defined by legislation and court decisions:
<ul style="list-style-type: none">▪ personal reasons: the employee is not or no longer able to work (in particular due to long-term sickness);▪ behavioral reasons: severe misbehavior by the employee (often immediate dismissal without notice period), normally after prior warning (examples for severe misbehavior: theft, absenteeism, drug abuse at work);▪ business reasons: plant downsizing or closure; in case of business reasons, the employer has to check all options for continuing employment, e.g. through reorganization; workers to be dismissed have to be selected according to social criteria ("Sozialauswahl"), i.e. years of service, age, family obligations, handicaps.

Employees can file a lawsuit against dismissal. This usually does not result in continued employment but in an agreement on severance pay. Since 2004, employees are entitled to severance pay of 0.5 monthly salaries per year of service in case of dismissal for business reasons if they do not go to court. The dismissed worker can thus opt for severance pay offered by the employer or file a lawsuit in order to get higher severance pay (Jahn 2005). There are special provisions regarding collective dismissals according to the size of the firm and the number of dismissals. When about 25% of the staff in a smaller firm are concerned, or the number of terminations exceeds 30 employees, not only the works council, but also the local BA office has to be informed at least a month earlier. In the recent past, in cases where firms met a difficult economic situation, trade unions and works councils agreed on concessions regarding working time and wages in exchange for the employer forgoing mass redundancies (firm-level "alliances for jobs", see Rehder 2003).

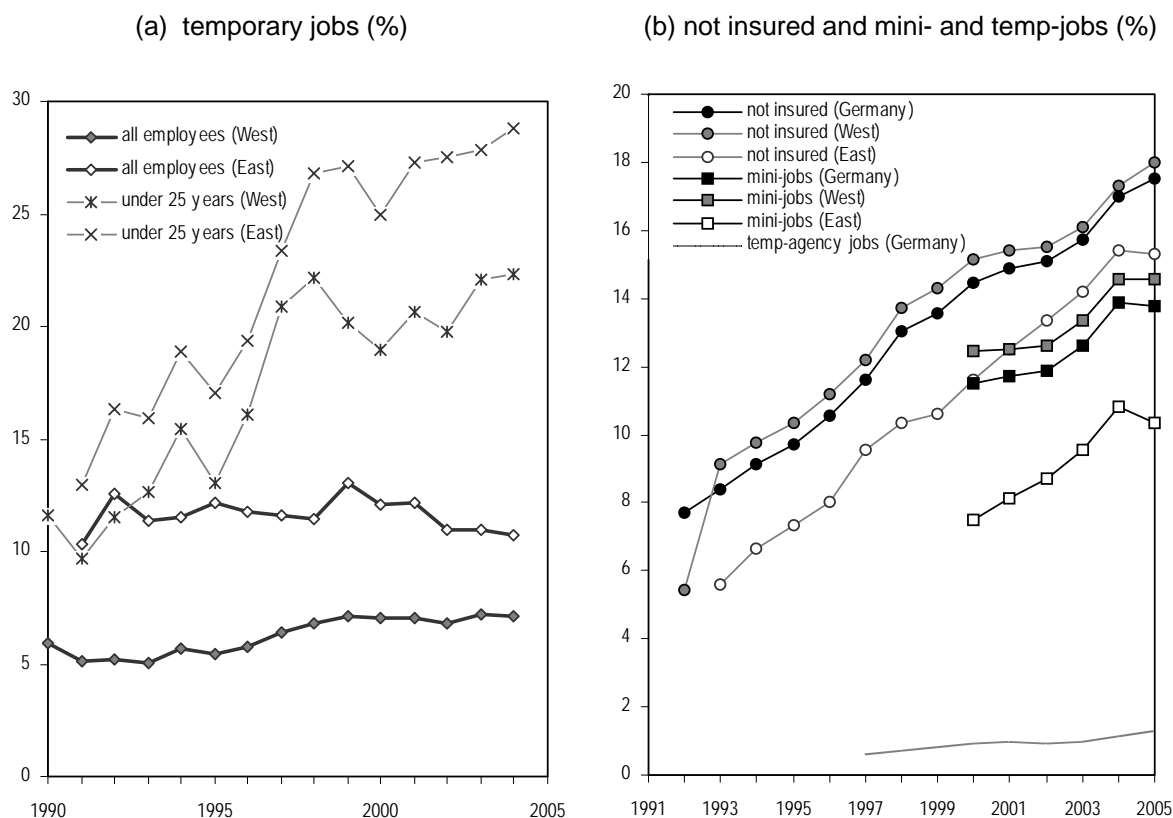
2.3 Fixed-term Contracts

A specific law (*Teilzeit- und Befristungsgesetz*) regulates fixed-term contracts. According to legislation, such temporary employment is possible if a valid reason is given: temporary demand for additional labor, termination of vocational or academic training, replacement of permanent staff, specific character of task, extended trial period or availability of temporary funds only. Fixed-term employment without any (valid) reason is only possible for a maximum period of two years (four years in case of enterprise creation). The employer cannot reemploy the same individual after a

fixed-term contract terminated without valid reasons. Deviation is possible through collective agreements. However, fixed-term employment without valid reasons was unrestricted in case of older workers of age 52 or over but this provision was nullified due to age discrimination by ECJ in fall 2005 and has to be newly legislated. Fixed-term employment terminates automatically without formal dismissal at the end of the period. However, during the duration of a fixed-term contract, employment stability is relatively high. Usually, there is no severance payment in case of expiry of fixed-term jobs, but employees leaving fixed-term employment are entitled to unemployment insurance, except for civil servants on fixed-term contracts, who receive severance pay (one month per year of service).

Temporary employment contracts (other than mini-jobs) are still relatively rare with only about 10% of employees in Germany in 2005. Half of this share consists of vocational training contracts. Hence, there are only about 5% genuine fixed-term contracts. By 2005, 7% of employees in West Germany have a limited contract and around 12% in East Germany. There has been only a slight increase in these contracts in West Germany and smaller changes around a constant level in East Germany (see Figure 3). However, such fixed-term contracts have increased substantially among young employees in both West and East Germany. Every fourth young employee under 25 years of age in West Germany has such a job entry contract and nearly every third one in East Germany. Temporary contracts are the norm for employment during firm-based vocational training in Germany. Thus, the share is particularly high among the very young (under age 25). Migrants are also overrepresented in temporary employment. In addition to training, subsidized jobs (ABM) particularly in East Germany account for about every fourth temporary job in 2000, many of which can be found in agriculture and the public sector (Jahn 2002). Although these temporary jobs are largely for the lower qualified and job starters, public universities employ junior academic staff on temporary contracts for up to 5 years under normal employment laws (or for up to 12 years under new rules for doctoral and post-doctoral researchers).

Figure 3: Temporary and mini-jobs by age group, Germany 1990-2005



Notes: (a) temporary jobs (*befristete Verträge*) in % of employees (including vocational training); (b) non-unemployment-insured, mini-jobs (*geringfügige Beschäftigung*), and temp-agency workers (June) in % of dependent employment.

Source: Mikrozensus 2004; (a) IAB Fibel; (b) own calculations.

2.4 Temp Agency Work

Employment in a temporary work agency (TWA) falls under the general regulations of either fixed-term or open-ended contracts in Germany, though in most cases, “temp” agency employment (*Zeitarbeit*) contracts between employees and TWAs are often open-ended, while the posted work assignments (*Arbeitnehmerüberlassung*) are task-related, i.e. fixed-term contracts between TWAs and the receiving firms. Agency work was also subject to additional restrictions in the past, such as maximum duration of individual postings or a ban on the synchronization of the contract with the agency and the actual posting. The posted work period was extended stepwise from three to six months in 1985, further extended to nine months in 1994, to twelve months in 1997, to 24 months in 2002, and finally the limit was completely abolished in 2003. The most recent changes implemented with the Hartz reform package removed virtually all remaining restrictions – except the ban on TWA activities in the construction sector. However, agency workers are entitled to the same wages and working conditions as regular staff (“equal treatment”). Deviations are only al-

lowed in the case of hiring unemployed people or if collective agreements exist, triggering several collective agreements between trade unions and TWAs on wages and working conditions.

The number of temp-agencies has nearly doubled from 8,700 in June 1997 to nearly 15,900 in June 2005 and temp-jobs (*Leiharbeit*) have more than doubled from 212,000 to 453,000 during the same period. Particularly the reforms in 1985, 1994 and 1997, and recently the 2002/03 reforms, led to substantial increases (Antoni/Jahn 2006). Given the short duration of employment (only 40% of jobs last longer than three months in 2003), there is a high turnover with 738,000 temp-jobs being created and nearly as many terminated in 2005. In West Germany, about 63% of temp-agency workers in 2003 were previously un- or non-employed, while 53% had no subsequent employment after the temp-contract (either another “temp” agency job or other employment). The recent surge in such jobs can be seen as one measure of flexibilization. Employers use temp-agency workers to overcome short-term demand peaks instead of hiring workers on normal employment contracts.

2.5 Mini-jobs

Another element introducing additional employment flexibility is low level part-time work not covered by full social insurance contributions. Although it is not differentiated in terms of employment protection in a narrow sense, it allows employers to reduce labor costs. The most recent reform implemented in 2003 increased the maximum earnings of those “marginal jobs” or “mini-jobs” to 400 € per month. While the employer has to pay full social security contributions and a lump-sum tax, amounting to 25% (as of mid-2006 30%) of the gross wages, earnings from mini-jobs are tax- and contribution-free on the employee’s side. This marginal job arrangement (*geringfügige Beschäftigung*), however, is not an entirely new instrument of labor market flexibility but has recently grown in importance. Until 1999, mini-jobs were not covered by social insurance, but the employer was obliged to pay a lump-sum tax. Thereafter, social insurance coverage was introduced, but the lump-sum tax was lowered in return. As of 1999, a second mini-job could no longer benefit from the tax and contribution exemption, but the option of tax- and contribution-free second jobs was reestablished in 2003, leading to an increase by one million secondary mini-jobs within two years. While mini-jobs are treated differently with respect to social security, there are no special rules or exemptions regarding labor law and employment protection.

Mini-job employment among those persons with only one job has increased from an estimated 2 million in 1991 to 4.7 million in 2005, not counting about 1.7 million additional secondary mini-jobs. Although a general social insurance levy (collected by the sickness funds) has been introduced, these jobs are exempted from unemployment insurance coverage. As figure 3 shows, about 14% of West German and 10% of East German employees hold a mini-job as their only source of employment income in Germany. Furthermore, additional mini-jobs may serve as second jobs in which employees would be covered by their first job; this is particularly the case for men. Married women with children profit from mini-jobs as they are insured via their husband and earnings are jointly taxed. Students and pensioners also tend to work on mini-jobs due to income limits for student grants and pensions. Thus, the share of mini-jobs increases in the older age groups in pre-re-

tirement and normal retirement age at 65. Given the decline in employees with social insurance (and excluding tenured *civil servants*, who are not covered by social insurance but through direct state payments), there has been a growing share of non-insured employees who were not covered by unemployment insurance, particularly those with mini-jobs and temporary contracts for civil servants (see Figure 3).

2.5 Self-employment

Self-employment (or independent employment) is an alternative to dependent employment and in general a more flexible arrangement as it is not covered by dismissal protection and other labor law provisions. There is also no compulsory social insurance for the self-employed in Germany, though there is voluntary access to social insurance and compulsory coverage by specific schemes in some professions. Immediately after unification, independent employment (both self-employment and helping family members) was higher in West Germany (10.1%) than East Germany (6.8% of all employed in 1992), yet it increased to over 11% in both parts of Germany by 2005. Given the relatively high burden of non-wage labor costs and regulations, self-employment is considered an option of circumventing some of the rigidities and costs of dependent employment. This led to an expansion of self-employment without dependent employees and often only one single client due to the “outsourcing” of services by firms.

To stop this potential threat of undermining dependent employment covered by social insurance, the red-green coalition government restricted “bogus” self-employment (*Scheinselbstständigkeit*) by law as of 1999, forcing such “quasi-dependent” employment to be covered by social insurance. False self-employment is defined (SGB IV §4, para 7) as self-employed work which is dependent on one main client, if the self-employed does not search for other clients and works at predefined hours and similar tasks as employees of the main client. However, to further labor market flexibility and strengthen business creation, most of these provisions were revoked in 2003. In addition, as a complement to stronger subsidization of business start-ups through active labor market policies, the requirement of a craftsman’s diploma was abolished in some of the craft professions at the same time. The quasi-dependently employed are obliged to pay social security contributions. Yet among the 238,000 self-employed who were insured by the public pension insurance in 2004, only 20,868 were forced by law and 28,113 were self-employed in “Me Inc.” (“Ich-AG”) start-ups under the Hartz reforms (DRV 2006).

2.7 Job Tenure

The impact of the relatively high level of employment regulation and the relatively marginal role of flexible employment has led to a high average duration of an employment spell in Germany in comparison to flexible Anglophone and Danish labor markets (Eichhorst/Thode/Winter 2004). Job tenure, the duration of employment with the current employer, is higher in West than in East Germany, although employment tenure increased after unification as those who remained in gainful employment stayed in the same job. Job tenure is higher among men than women and among

Table 3: Job duration by gender and age group (2004) (% of employees)

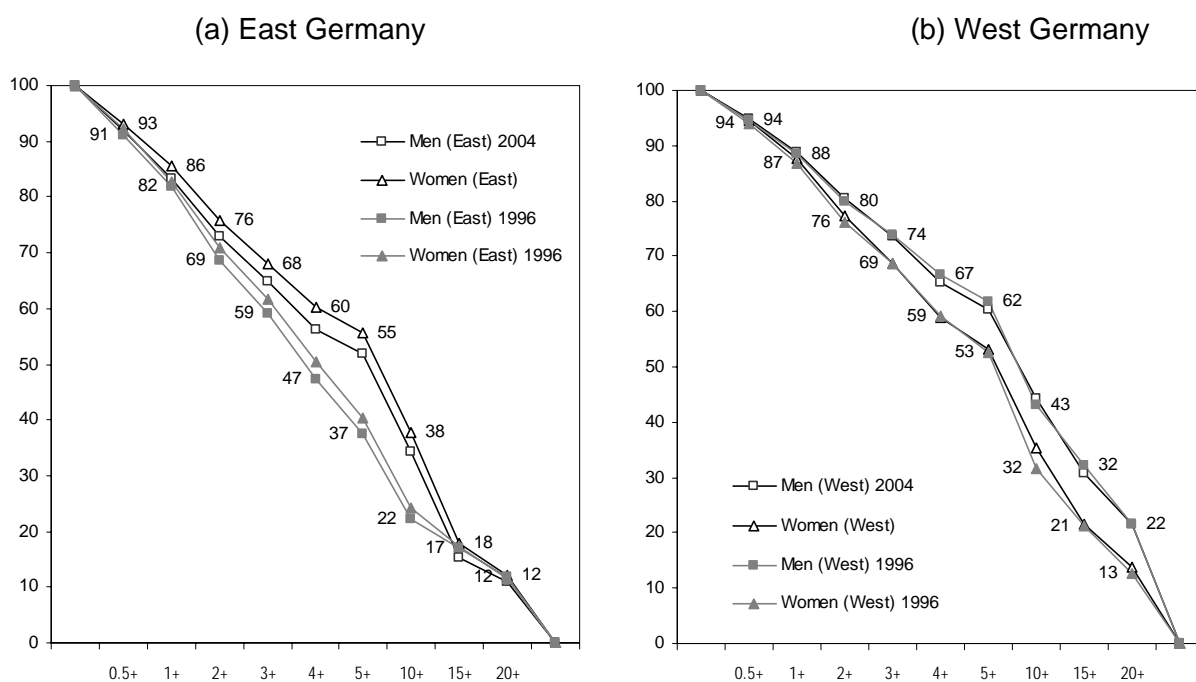
	Age	Men				Women			
		-1y	1-5y	5-10y	10+y	-1y	1-5y	5-10y	10+y
Germany	15-24	37.3	51.4	11.1	0.2	36.2	51.9	11.7	0.2
	25-54	10.8	22.4	20.8	46.1	11.6	25.9	21.9	40.6
	55-59	3.9	9.1	9.6	77.3	4.5	12.5	14.1	68.9
	60-64	3.2	7.4	8.6	80.8	4.1	11.6	13.2	71.1
	Total	12.5	23.4	18.2	45.9	13.6	27.3	19.8	39.3
Netherlands	15-24	28.1	57.7	14.0	0.2	29.6	59.7	10.7	0.0
	25-54	5.5	28.2	24.2	42.1	6.0	35.3	26.3	32.5
	55-59	1.8	8.4	11.0	78.8	2.0	14.9	15.1	68.1
	60-64	1.3	10.6	11.7	76.4	0.0	9.6	14.5	75.9
	Total	6.9	28.1	21.4	43.6	8.1	36.0	23.6	32.4
United Kingdom	15-24	46.5	43.8	9.6	0.0	47.6	44.6	7.7	0.1
	25-54	14.2	28.6	21.5	35.7	15.5	33.0	23.0	28.6
	55-59	9.0	19.6	18.3	53.1	8.0	18.6	19.9	53.5
	60-64	7.6	18.1	19.0	55.4	7.0	16.3	23.2	53.5
	Total	17.6	28.9	19.4	34.1	19.1	32.5	20.4	28.0

Source: OECD Database (2006), based on EU labor force surveys; own calculations.

those with occupational training than those without it. In fact, comparative studies indicate that Germany (as well as Japan) has higher job tenure rates and steeper age-related retention rates due to the firm-based vocational training and the importance of the entry-job in rather internal-labor-markets (OECD 1993). Germany has a higher share of prime work age workers (25-54) who have been employed for more than ten years by the same employers (46% of men and 41% of women) compared to the Netherlands (42%/33%) and the United Kingdom (36%/27%). Job tenure is particularly high among older workers (55+), who are protected against dismissal after 10-15 years of service under most collective agreements (see Table 3).

A large share of employees in 2004 has been employed for more than one year (86% of East Germans, 88% of West Germans). The majority of employees has been employed for more than five years: around 55% of men and women in the East as well as West German women, and again West German men have an even higher rate (62%). While the gender differences remained stable, that is, men on average have longer tenure than women in West Germany, the difference is much smaller in East Germany. While tenure has increased in East Germany over the last decade as a result of more stable employment relations after the transition to a private market economy, hardly any change is observable in West Germany. This cross-sectional analysis indicates the long-term relationship for most employees, except for those with mini-jobs and fixed-term contracts. Moreover, interruptions of employment due to unemployment probably much less affect those working in core employment segments than those in rather flexible segments of the labor market. Given the high level of employment protection, turnover in the labor market remains rather low in Germany, thus providing fewer opportunities for the unemployed to find job openings.

Figure 4: Job tenure in years (survival curve), Germany 1996 and 2004



Notes: Cumulative share of employees by duration of current job of (full-time and part-time) employees, excluding mini-jobs.

Source: Mikrozensus 1996 and 2004; own analysis and calculations

2.7 Responsibility

Dismissal protection is regulated by national legislation, court decisions and collective agreements. Employment protection is mainly an issue of national legislation. Since labor market insiders have a strong position in politics (through the workers wing in the Social-Democratic and Christian-Democratic parties) and due to the institutionalized role of trade unions in the industrial relations arena, they tend to defend the status quo of dismissal protection. Court-made jurisprudence plays a major role in defining the concrete substance of dismissal protection, the level of severance payments or the regulation of fixed-term employment. Dismissals can be nullified by Labor Courts (*Arbeitsgerichte*); this regularly leads to agreements on severance pay. Employees who are organized union members can be represented by trade union officers before the court, others rely on lawyers. Works Councils have to be consulted in all cases of dismissals. Dismissals of disabled people need authorization by the BA. Notifying the BA is also required in case of collective dismissals.

Additional provisions stem from collective agreements. Collective agreements frequently provide for additional employment protection favoring older employees on regular contracts with long tenure. Hence, both extended notice periods and higher severance payments, but also the de facto exclusion of dismissals for employees with longer tenure, can be introduced through collective agreements. Collective agreements are always a complement topping up legislated dismissal protection and cannot substitute for it since national legislation provides a binding minimum.

Hence, collective agreements provide even stronger dismissal protection than employment protection in national legislation. Sectoral collective agreements and enterprise-level agreements to secure employment (*Standortbündnisse*) strengthen insider protection over the interests of outsiders, with the exception of the promotion of vocational training. There is a growing tendency to circumvent statutory employment protection through self-employment, free-lancers as well as mini-jobs and fixed-term contracts or by using temporary agency work. This basically reflects employers' preferences, not necessarily those of employees. Flexibility of the German labor market is not enhanced via deregulation of dismissal protection but through relaxing alternative forms of (marginal) employment.

Table 4: Major reforms in dismissal protection, fixed-term contracts and temporary agency work

Year	Details
1993	Notice period for blue-collar workers was extended to align with that of white-collar workers (four weeks)
1994	Regulation of temporary employment for maximum period of 18 months is extended until 2000 (BeschFG 1994); new insolvency law facilitates dismissal of employees in case of insolvency; employees are protected from dismissals due to employers' obligation of continued payment of wages (EFZG, 05/26/1994)
1996	First substantial restriction of dismissal protection: Dismissal protection only applies to businesses employing at least 10 workers instead of 5 (BeschFG 1996); part-time workers are taken into account, but only according to their amount of weekly working hours relative to full-time workers; criteria for social selection are restricted; high-performing employees can be withdrawn from the social selection process; options for fixed-term contracts are liberalized; making use of "Old-Age Part-time Work" is not a dismissal and cannot be negatively taken into account in a social selection procedure; renewal period for FTC and TWA and frequency of renewals were increased: maximum period for temporary employment increases from 18 to 24 months and temporary contracts can be extended up to 3 times within this period; temporary contracts can be concluded without particular reasons with employees over 60.
1999	Restriction of dismissal protection from 1996 is cancelled to large extent: Dismissal protection applies to firms employing at least 5 workers again; social selection criteria are extended ("Korrekturgesetz" 1999)
2001	"Part-time and Temporary Work Law" (TzBfG) comes into effect, which allows temporary work contracts of up to a total of 2 years <u>only</u> for new hires; temporary contracts can be concluded without reasons with employees over 58 (previously 60); ban on discrimination between temporary and permanent employees
2004	Old limit (of 1996) up to which the business remains unaffected by dismissal protection is reestablished; size threshold is increased from 5 to 10 employees again (Agenda 2010), but increase only applies for new hires. Part-time employees are no longer counted; criteria for social selection are restricted once again. Dismissed employees can opt for compensation through severance pay instead of having the right to file a lawsuit; limit on the maximum total duration of TWA postings was lifted (from 2004), but principle of equal treatment of regular staff and TWA staff now applies unless there is a collective agreement regulating wages and working conditions of TWA staff.
2006	Tax exempt amounts regarding taxation of severance pay (in case of dismissal) are abolished unless the compensation was arranged before January 2006 and the compensation itself is due before January 2007.

Source: authors' compilation.

2.8 Special Schemes and Collective Agreements

Sectoral arrangements are most prominent in the following cases: (1) there is relatively strict employment protection in the public sector. This not only applies to civil servants on permanent contracts, who can hardly be dismissed at all, but also to public employees with a private law contract. If there is an open-ended contract, public employees over 40 cannot be dismissed after 15 years of service. This, however, leads to a tendency of increased use of fixed-term contracts in the public sector regarding both fixed-term contracts with civil servants and public employees. (2) The situation is different in tertiary education (*Hochschulrahmengesetz*), where special rules apply for doctoral and post-doctoral research positions (two times six years of fixed-term contracts). (3) There are particular sector and firm-level-agreements in the private sector (such as metal, chemical industry) in which job security agreements are signed to exchange employment security for pay restraints. Many collective agreements include special clauses for employment protection of older workers (usually above 40 or 50) and long serving workers (with tenure of 15 or 20 years and more). According to collective agreements collected by the Federal Labor Ministry in 1996, 56% of employees covered by collective agreements were under such provisions, while it was only 23% in the mid-1980s (Jahn 2003). Recent collective agreements (2005) includes employment protection from age 50 onwards and 10 years of service in the banking sector, from 53 years onwards and 15 years in larger shops, and from 53 onwards and 3 years in the pilot agreement of the metal manufacturing industry (Bispinck 2005).

3 UNEMPLOYMENT INSURANCE

3.1 Recent Development

Regarding unemployment benefit systems, there is a dual tendency over time: on the one hand, a high degree of institutional continuity characterizes unemployment insurance, on the other hand, in unemployment assistance, the move from a means-tested but earnings-related benefit (*Arbeitslosenhilfe*) to a flat-rate benefit (*Arbeitslosengeld II*) in 2005 marks a major institutional change. In this sense, the “Bismarckian” features of the German social insurance-based welfare state have been weakened. This is also true given the fact that the range of the insurance regime is shrinking due to subsequent cuts in unemployment insurance benefit (*Arbeitslosengeld I*) duration (the most relevant one reducing unemployment insurance benefits from 32 to 18 months for workers aged 55 and over has been in effect since early 2006) and a growing portion of the long-term unemployed relying on unemployment assistance. The abolition of earnings-related unemployment assistance was part of a major policy shift from a passive orientation of labor market policies to activation. Although potentially activating provisions had been embodied in earlier legislation, the most recent changes resulted in an “awakening” of these “sleeping” principles and the creation of new administrative structures in order to implement activating policies more effectively. Although the Hartz reforms from 2003 to 2005 can be seen as a “big bang” of activation policies in Germany,

there have been some minor changes in this direction in the late nineties which have made access to unemployment benefits stricter and more selective. One major step was the withdrawal of occupational protection in 1997. Requalification for unemployment insurance benefits through participation in active schemes was abolished for training programs in 1998 and for direct job creation and other schemes in 2004.

3.2 Coverage

In Germany, unemployment insurance is compulsory for nearly all employees in both the private and the public sector. This basic structure has been stable for the relevant time horizon. Compulsory unemployment insurance covers all private sector employees with some exceptions. Some groups can opt for continuous coverage by unemployment insurance if they were covered in the period immediately before this status change (*Versicherungspflicht auf Antrag*). This applies to people providing personal care and to the self-employed, but also to insured persons who migrate to non-EU countries (in case of the self-employed only until 2010). Apart from these options of continued insurance, voluntary adhesion to unemployment insurance is ruled out. In addition, there are no private providers of alternative unemployment insurance.

Table 5: Coverage of unemployment insurance

Covered by unemployment insurance (§§ 24 – 26 SGB III):
<ul style="list-style-type: none"> ▪ part-time workers (except minor jobs with earnings below 400 € per month); ▪ trainees in dual vocational training; ▪ employees on leave during compulsory military or civil service; ▪ employees on sick leave or parental leave; ▪ employees in the public sector with a private law contract (i.e. exemption of civil servants only).
Excluded are (§ 27 SGB III):
<ul style="list-style-type: none"> ▪ civil servants benefiting from life-long employment guarantee; as a consequence, there is no voluntary insurance against unemployment for civil servants; ▪ civil servants with fixed-term contracts (e.g. assistant professors, public officeholders, soldiers); ▪ pupils and students; ▪ the self-employed; ▪ company board members (managers); ▪ interns and fellowship holders; ▪ employees in minor jobs below 400 € per month (“mini-jobs”); ▪ people 65+ (this will have to be changed as pension age moves to 67); ▪ permanently disabled people no longer available to the labor market;

3.3 Entitlement Conditions

Entitlement to unemployment insurance benefits requires meeting the following conditions: (1) unemployment insurance benefits can only be received after prior employment of at least 12 months within the last 24 months (recent reform), yet prior employment has to be covered by compulsory or voluntary unemployment insurance; (2) the unemployed have to register with the public employment service (PES) as early as possible. The unemployed are obliged to search for work on their own (though no rules as to how intensive this has to be) and to be available for job placement by PES and participation in ALMP schemes; regarding individual search activities, the unemployed have to use all options of reintegration into the labor market, in particular all activities resulting from the reintegration agreement (*Eingliederungsvereinbarung*) with PES, services provided by third parties (e.g. private job placement agencies) and self-information services provided by PES; the unemployed are considered as available for PES activities if they are able to take up jobs of 15 hours per week or more under usual conditions, willing to follow all advice and recommendations by PES and willing to take up suitable jobs and participate in ALMP programs.

Unsuitable are job offers that pay significantly less than the earnings in prior employment. During the first three months, the unemployed can reject jobs offering less than 80% of prior earnings, thereafter less than 70% until the sixth month of unemployment, and finally after six months of unemployment, all jobseekers have to accept jobs providing net earnings equal to or higher than unemployment insurance benefits. The unemployed have to accept certain commuting times (normally 2.5 hours per day). Unemployed singles are expected to move after four months of unemployment if this allows them to take up a new job (or earlier if reemployment is not expected within commuting distance). The older unemployed (58+) do not have to be available for work or look for work in order to be entitled to unemployment insurance benefits. PES urges them to apply for old-age pensions as soon as possible (§ 428 SGB III). This was possible due to the pension for unemployed people at age 60, until recent reforms increased the age limit from 60 in 2006 to 63 by 2008, while those born after 1951 will not profit from an earlier drawing at all.

Unemployed persons not eligible for unemployment insurance benefits due to expiry of this benefit or lack of sufficient contribution period are entitled to means-tested unemployment assistance (*Arbeitslosengeld II* or ALG II) if they are between 15 and 65 years of age; capable of working at least 3 hours a day; pass a means test and are willing to accept any work (with few reasons to reject job offers) or public employment opportunities (relief work, "One Euro Jobs"). Unemployment assistance (ALG II) cannot only be received after expiry of unemployment insurance benefit, but also if an unemployed person has never been entitled to unemployment benefit (e.g. due to lack of sufficient prior employment, after longer periods of self-employment or former temporary civil servants). ALG II not only provides minimum income for the unemployed (suggested by the official term *Grundsicherung für Arbeitsuchende*) but also for the self-employed or people in dependent employment with low earnings. They can receive ALG II as an earnings supplement. In that sense, ALG II provides a national minimum income for all employable people without sufficient resources. Older beneficiaries (equivalent to the clause in unemployment insurance) and employ-

able persons who take care of small children or elderly persons are exempt from the job search requirement under ALG II.

Regarding sanctions, the unemployment insurance benefit (ALG I) is suspended after voluntary quitting or in case of insufficient job search efforts, refusal of a suitable job or participation in ALMP or in case of delayed registration with the BA. Suspensions last between one week and twelve weeks. Concerning ALG I, in addition to sanctions for refusal of job offers, participation in activation schemes or other infringements, non-acceptance of an integration contract or failure to meet the obligations agreed on also lead to benefit cuts, as does concealing information on income or wealth. In contrast to unemployment insurance, sanctions in unemployment assistance result in ALG II being reduced by 30% (with the temporary supplement suspended). Repeated misconduct within one year results in further reductions of ALG II by 60% or even a total suspension or a replacement of cash transfers by benefits in kind. Sanctions last for three months. Benefits for young people can be restricted to housing and heating. Sanctions are implemented by the BA in case of ALG I and by the bodies responsible for ALG II administration (joint bodies by BA and municipalities – *Arbeitsgemeinschaften* – or, in some districts, the municipality alone) and can be contested by filing an internal complaint or a lawsuit before a Social Court. Empirical data on sanctions are available for ALG I only, while nation-wide information on ALG II sanctioning is still missing. In 2005, about ten percent of all newly unemployed persons claiming ALG I unemployment insurance benefits were subject to punitive sanctions (150,000). However, about 76% of these sanctions were due to voluntary quits, 20% were sanctioned due to refusal of suitable work and only 4% after rejection of participation in ALMP schemes. In addition, about 110,000 unemployed were sanctioned after delayed registration with the PES. About six percent of all sanctions were repealed after complaint procedures or a court judgment. In general, the frequency of sanctions is relatively low despite a slight increase over time.

3.4 Benefit Levels and Duration

The unemployment insurance benefit (*Arbeitslosengeld I* or ALG I) is related to prior earnings and household type, maintaining the standard of living during previous employment. It provides 67% percent of insured *net* earnings (in the period relevant for the calculation of benefits, normally 12 months, after some minor adjustments to actual net earnings) for the unemployed with children, 60% in all other cases. Tax-free unemployment insurance benefits currently last for 6 to 18 months depending on age and prior employment duration. People below the age of 55 can obtain unemployment insurance benefits for a maximum period of 12 (6) months if they had been employed for at least 24 (12) months. People aged 55 and over can receive unemployment insurance benefits for 15 or 18 months if they had been employed for at least 30 months before unemployment. Until January 2006, the older unemployed were entitled to unemployment insurance benefit for a maximum period of 32 months. This cut in maximum benefit duration shortens the early retirement pathway of long-term unemployment benefit recipients which had become a popular early exit route since the 1980s.

Table 6: The pre- and post-reform of non-activity benefits in Germany (Hartz IV)

Old System (until 2004)	New System (2005 -)
<i>Arbeitslosengeld</i> (unemployment insurance benefit): funded through contributions, earnings-related, limited duration	<i>Arbeitslosengeld I (UB I)</i> : funded through contributions, earnings-related, limited duration
<i>Arbeitslosenhilfe</i> (earnings-related unemployment assistance): tax-funded, earnings-related, means-tested, infinite duration	<i>Grundsicherung (Basic income scheme for needy jobseekers)</i> <i>Consists of</i> <ul style="list-style-type: none"> a) <i>Arbeitslosengeld II (UB II)</i>: tax-funded, means-tested, flat rate, after expiry of UB I (and temporary supplement), infinite duration (integration of <i>Arbeitslosenhilfe</i> and <i>Sozialhilfe</i> for people capable of working) but stronger principle of activation b) <i>Sozialgeld</i> (social allowance) for children below the working age of 15 living in a household of an UB II recipient
<i>Sozialhilfe</i> (social assistance): tax-funded, means-tested, flat rate, infinite duration	<i>Sozialhilfe</i> (social assistance): means-tested, tax-funded for those working age people not capable of working and for needy persons above 65 years

In addition, employees covered by unemployment insurance are also eligible for alternative benefits in case of short-term unemployment if they meet specific criteria. This holds for bad weather payment (*Saison-Kurzarbeitergeld*) and additional benefits for construction workers (*Zuschuss-Wintergeld*, *Mehraufwands-Wintergeld* and subsidization of construction employers' social contributions) and for short-time work (*Kurzarbeit*) benefit in case of a temporary demand slump implying at least a 10% reduction in earnings, but only if this benefit is based on requests by the employer and works council. The BA pays 67% of reduced earnings up to the full 67% of past wages in case of no hours work (*Struktur-Kurzarbeitergeld*) to those who are de facto unemployed but fully eligible for unemployment benefits in case of later dismissal. This was relatively common in the early 1990s.

Hence, the unemployed without sufficient income from work, partners' earnings or income from wealth are entitled to unemployment assistance with infinite duration. It provides a basic allowance of 345 € p.m. and appropriate housing (incl. heating). Flat-rate *Arbeitslosengeld II* replaced earnings-related but also means-tested unemployment assistance (*Arbeitslosenhilfe* or ALH) by January 2005. The abolition of ALH means that there is now only one benefit system for the long-term unemployed that does not take prior employment and earnings levels into account. However, if recipients of unemployment assistance had been entitled to ALG I before moving to ALG II, they are entitled to a fixed-term supplement making up for two thirds of the difference between unemployment insurance benefit and unemployment assistance in the first year, and one

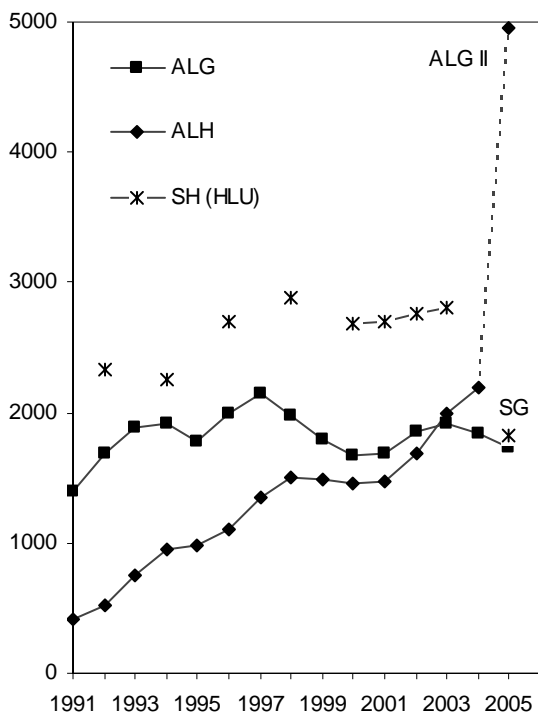
third of this difference in the second year so that the transition from (higher) insurance benefits to (lower) assistance is smoothed.

If there are two employable recipients of unemployment assistance, the individual benefit is 80% of the general benefit. Younger recipients below the age of 25 living on their own receive 80% or 90%. It has to be mentioned, however, that employed persons are also entitled to ALG II if their earnings are not sufficient to safeguard the social minimum income. This is particularly true for employees with low hourly earnings, but also for persons in marginal or part-time employment if there is no first earner in the household who provides substantial income. Given the fact that the social minimum threshold increases with household size (e.g. with the presence of a non-working partner or the number of children), the equivalent income from work required to pass this threshold also increases.

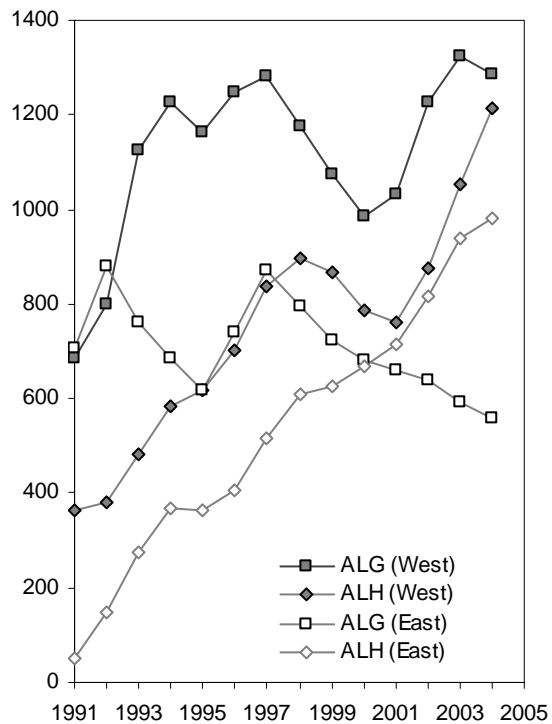
Since the 1990s, the number of transfer recipients has remained relatively stable in the case of unemployment insurance benefits (now ALG I) with only minor cyclical ups and downs in both West and East Germany, while the number of long-term unemployment assistance (ALH) recipients has increased substantially in Germany from below 0.5 million in 1991 to above 2 million in 2004. The fourth Hartz Reform has skyrocketed the number of unemployment assistance (ALG II) recipients to 5 million compared to former ALH and the employable social assistance recipients (mainly a statistical effect), while the social assistance to non-employable individuals and their dependents (*Sozialgeld*) are just below 2 million individuals (not comparable to former social assistance figures).

Figure 5: Number of transfer recipients (1000s), Germany 1991-2005

(a) Germany



(b) West and East Germany



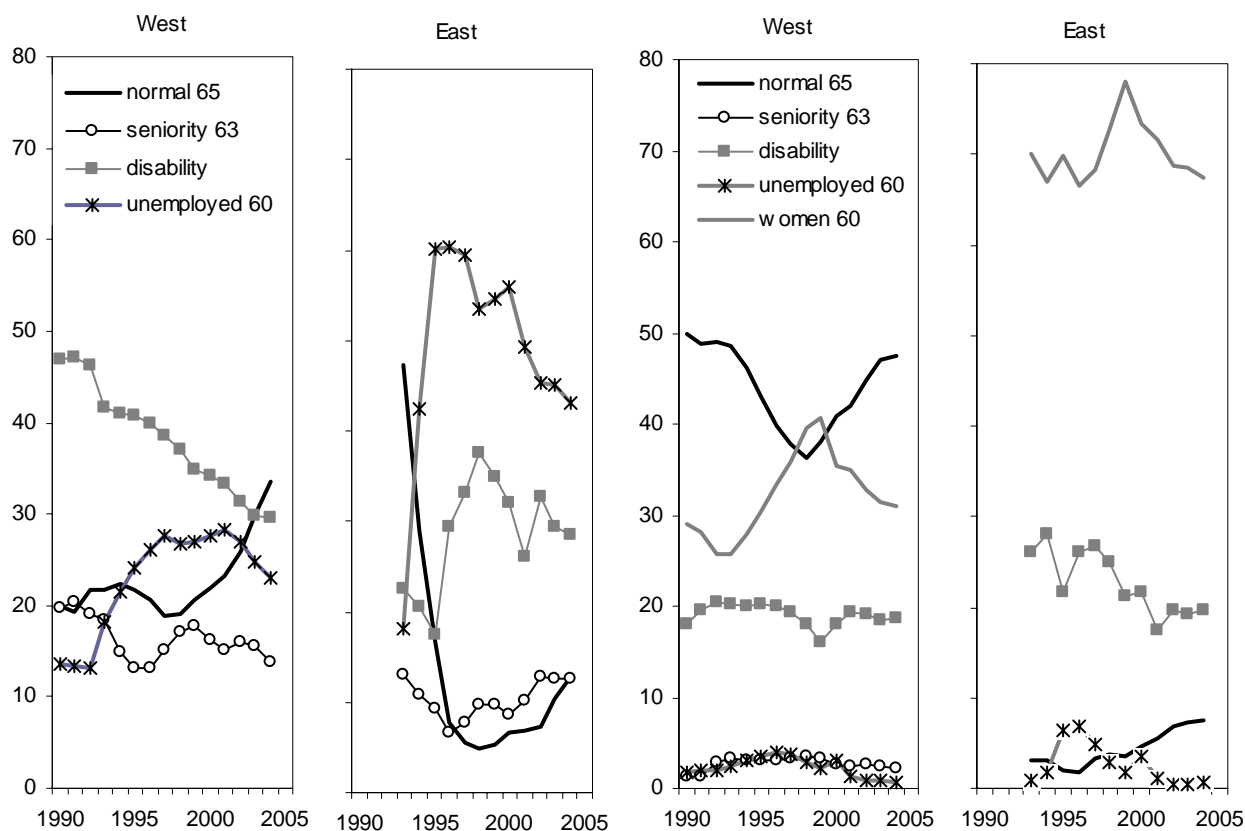
Notes: ALG: unemployment insurance benefits (*Arbeitslosengeld*); ALH: unemployment assistance (*Arbeitslosenhilfe*); SH (HLU): means-tested social assistance as income support (*Sozialhilfe: Hilfe für den Lebensunterhalt*), 2005 reform: ALG=ALG I; ALH=ALG II; SH: social assistance for the non-employable (*Sozialgeld*).

Source: BA data; Federal Statistical Office; German Council of Economic Experts.

Figure 6: New pensions for men and women (%), Germany (West and East) 1990-2004

(a) New pensions among men

(b) New pensions among women



Source: new pension claims (DRV).

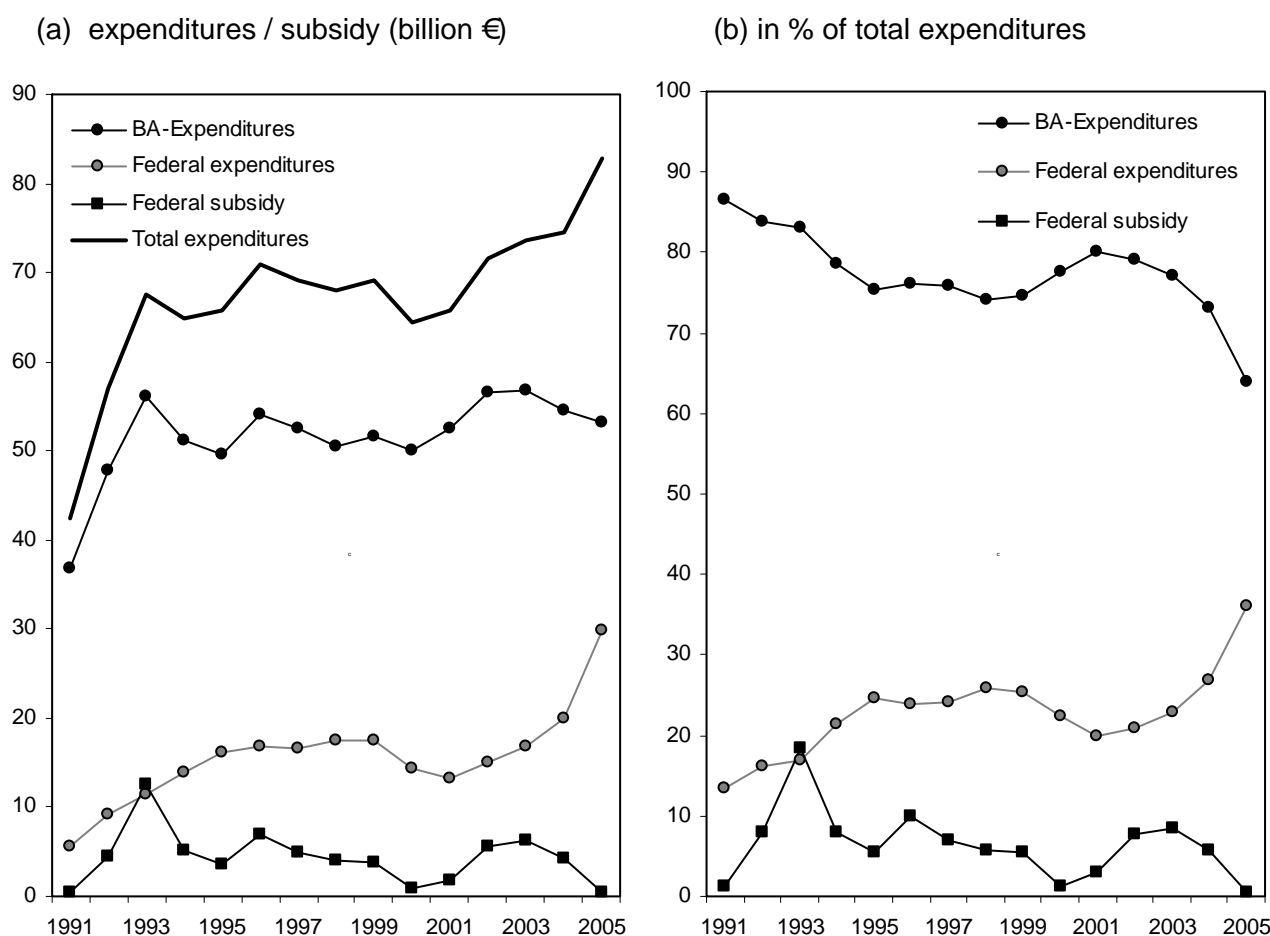
Alternative benefits are available to inactive persons such as (a) partial or full disability pensions (*Erwerbsminderungsrente*); (b) early retirement through early pension drawing (60+: due to unemployment, 63+ for long-term pension insured), have been or are being phased out for those born before 1951 and 1937 respectively; (c) social assistance (*Sozialgeld*) for non-employable people (*Nicht-Erwerbsfähige*) living in needy households (*Bedarfgemeinschaft*) with employable unemployed persons, i.e. sick and disabled people incapable of working at least 3 hours a day within the foreseeable future; children below 15. These pathways to early retirement have offered ample opportunities for labor shedding in Germany (Ebbinghaus 2006) until the pension reforms of the 1990s and 2000s as well as Hartz reforms are increasingly limiting these passive reductions of labor. Only a small but rising share of new pensioners exits the labor market at age 65, the age of the normal old age pension (see Figure 6). Three different disability pension schemes allowed among nearly half of West German men in the 1990s and about one third until today an earlier exit prior to 65, while a majority of East German men (and a quarter of West German men) were first unemployed for up to 32 months and then received the pension for the unemployed at age 60. The majority of women in West Germany enters retirement at age 65 today, while more than two thirds of East German women leave at age 60, following the pattern established in the GDR (see Figure 6), and so does about one third of West German women (many without long employment records).

3.5 Fiscal Aspects

Unemployment insurance - which provides resources for both unemployment insurance benefit, ALG I, and active labor market policy for recipients of ALG I - is mainly funded through social insurance contributions. Employees and employers share the contributions equally. The current contribution rate is 6.5% of gross wages (3.25% employee, 3.25% employers) up to an earnings ceiling that is adjusted annually (current earnings ceiling: 5.250 € per month/63,000 € p.a., West, and 4.400 € per month/52.800 p.a., East). Persons opting for voluntary continuation of insurance have to pay a lump-sum contribution. The federal government covers deficits through general taxation. Since unification, the contribution to UI was increased to 6.8% in April 1991, and remained at a stable 6.5% since 1993. Contributions to UI will be reduced by more than two percentage points to 4.2% as of January 2007. This will be financed by an increase in VAT and by efficiency gains within active labor market policies. The employer withholds employee contributions from the gross wage. Both employer and employee contributions are paid by the employer as part of comprehensive social insurance contribution (including pension and sickness insurance as well as old-age care insurance) to the sickness fund, which redistributes contributions to responsible bodies; in case of unemployment insurance to the BA.

Long-term unemployment assistance benefits (ALH, now ALG II) and related active labor market policies are tax-funded - mainly by the federal level, but the municipalities pay part of the housing benefit. The federal government also paid the former unemployment assistance. The federal government and municipalities jointly finance (through taxes) expenditures of the long-term unemployed for housing and heating. Municipalities pay for auxiliary reintegration services provided to the long-term unemployed (such as advice in case of private debts, drug problems). For each recipient of ALG I who becomes long-term unemployed and is transferred to ALG II, the BA has to pay approx. € 10,000 to the federal government (*Aussteuerungsbetrag*).

The large share of the total revenues of around 68 billion in 2004 consisted of contributions of 50 billion (74%), while the federal government paid around 17 billion (25%) for unemployment assistance (ALH) and an additional subsidy to balance the deficit (6 billion in 2004). While the BA revenue contribution to the BA's expenditures was relatively stable given the stagnant income from social contributions, the federal contribution increased with the growth of long-term unemployment and, thus, unemployment assistance payments. Moreover, there is a cyclical up and down on federal subsidies towards the BA's deficit depending on the business cycle. By the mid-2000s, when the Hartz reforms changed the BA's labor market policies, the total expenditures had already increased significantly to the detriment of the federal contribution and subsidy. Declining receipt of unemployment insurance benefits, but also fewer insurance participants in ALMP, means a reduction in expenditure under the insurance scheme (SGB III), whereas benefit receipt and expenditure expand under the assistance scheme (SGB II), i.e. for unemployment assistance and associated ALMP schemes. In 2006, this will lead to a surplus in the BA system (SGB III) of about 10 billion €, while at the same time expenditure in the tax-funded unemployment assistance program will be about 10 billion € higher than expected (Kaltenborn/Schiwarov 2006).

Figure 7: BA and federal expenditures and subsidy, Germany 1991-2005

Source: BA Arbeitsmarktstatistik, BA Geschäftsbericht; Trampusch.

3.7 Sectoral Schemes

The system of unemployment benefits in Germany is a general one covering all regions and sectors, only excluding civil servants who usually obtain life-long employment tenure. There are no additional sectoral unemployment insurance schemes. However, one has to mention some specific features: in case of dismissals or collective redundancies, severance payments frequently top up unemployment benefits and in some cases provide a bridge to early retirement. In 1997, crediting of redundancy payments against unemployment benefits was introduced but abolished again in 1999. Favorable tax treatment of severance pay was revoked in 2006. Civil servants on fixed-term contracts are entitled to a specific severance payment (*Übergangsgeld*). They receive severance pay depending on the duration of prior employment (one month for each year of service). In addition, there is a sectoral scheme in the construction sector that aims at stabilizing employment and earnings in case of bad weather.

There is a special scheme of contributions (*Winterbeschäftigungs-Umlage*) by construction firms (1.2%) and employees in this sector (0.8%) to finance additional benefits complementing "Saison-Kurzarbeitergeld" financed by general contributions. A sectoral bipartite body (SOKA-BAU) col-

lects benefits to this regime (about 0.2 billion € per year). In addition, employers have to pay, via the Berufsgenossenschaft, into a fund for insolvency benefits (about 2 billion € per year). Additional revenues are received from the EU social fund (ESF) (about 0.3 billion € per year).

3.8 Responsibility

Unemployment insurance and unemployment assistance are regulated by national legislation. Hence, there is a unified legal framework. Social partners can influence policy-making and – to some extent – have a say in actual implementation of the benefit system through the Federal Employment Office (*Bundesagentur für Arbeit*, BA) governed by the principle of self-administration, but this influence was curtailed significantly with the Hartz reforms. The main body of social partner influence now is the tripartite supervisory board (*Verwaltungsrat*), which is responsible for supervising the BA executive board, approving the annual budget and the annual business report. The supervisory board can also request additional information, internal audit reports or external review. In addition, and most importantly, the supervisory board has to approve the business objectives of the BA management. In this respect, the most recent shift towards effectiveness and cost efficiency in BA resource allocation is also due to political support by the supervisory board. There are no social elections in this social insurance, instead representatives are nominated by the social partners and government. Neither do competing providers of unemployment insurance exist.

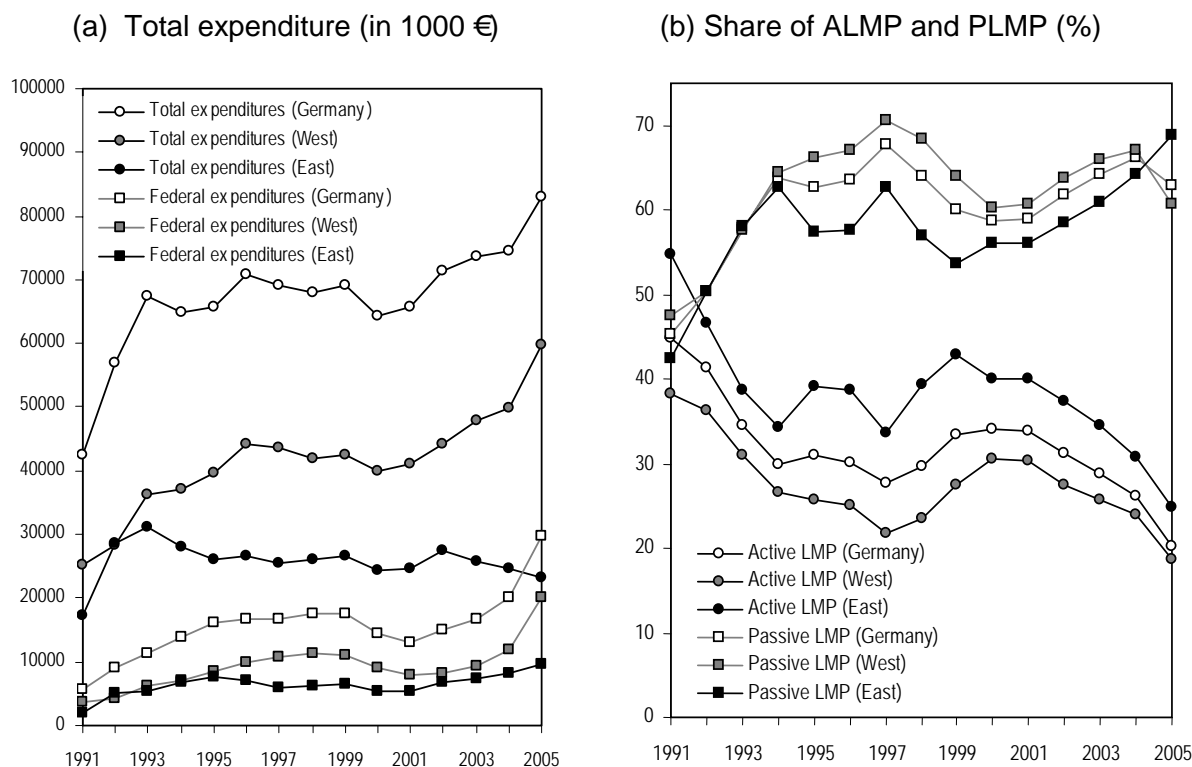
The BA is not only responsible for the administration of unemployment insurance benefits but also for the delivery of job search assistance (PES), counseling and active labor market policies (see below). There had been a division of responsibilities in terms of unemployment and social assistance in the past: the BA administered unemployment assistance on behalf of the federal governments, while the municipalities were responsible for the funding and the administration of social assistance. The merger of unemployment assistance and social assistance for employable persons through Hartz IV was accompanied by a reorganization of the bodies administering benefits and activation measures for the recipients of ALG II. In formal terms, the BA is responsible for administering unemployment assistance and activating schemes, the municipalities for housing and heating as well as for auxiliary social services. However, for practical implementation, there are joint bodies of BA and the municipalities (*Arbeitsgemeinschaften* or ArGe) in most districts. In 69 districts, however, the municipalities have taken over the complete administration of ALG II and active schemes on an experimental basis (*Optionskommunen*, see below). BA, ArGe and *Optionskommunen* have some leeway regarding “activation” and supervision of jobseekers but not regarding entitlements to unemployment benefits, which are highly formalized in legal terms (“verrechtlicht”).

Severance pay is a functional equivalent to experience rating in unemployment insurance, as it is proportional to tenure and wage level (and the frequency of dismissals). Since there is no differentiation of contributions to unemployment insurance by sector or firm that reflect the frequency of dismissals, sectors and firms with high employment protection and tenure (classical manufacturing) subsidize sectors and firms with frequent unemployment spells through their unemployment insurance contributions. However, the opposite is the case with regard to early retirement,

where unemployment insurance and old age and disability pensions provide benefits to redundant older workers in larger firms, particularly in manufacturing.

In comparison with other segments of social insurance, such as sickness insurance or old age / disability pension insurance, the role of the social partners is more restricted in unemployment insurance. Unemployment insurance and active labor market policies within the framework of the BA do not have bipartite but tripartite supervisory structures also involving the government directly. Sickness funds are in a way a unique feature in German social insurance as there is a limited amount of competition between different funds that have some leeway in fixing the contribution rate autonomously and in offering additional benefits supplementing the catalogue defined by national legislation. Social partners used pre-retirement and disability pensions (both parts of the old age pension system) for early retirement, i.e., the externalization of restructuring costs to the social insurance system. They could rely on options provided by national legislation (which was influenced by the social partners) such as several early retirement schemes, early access to old-age pensions after unemployment and old-age part-time work.

Figure 8: Expenditures for labor market policy in Germany (1,000 €)



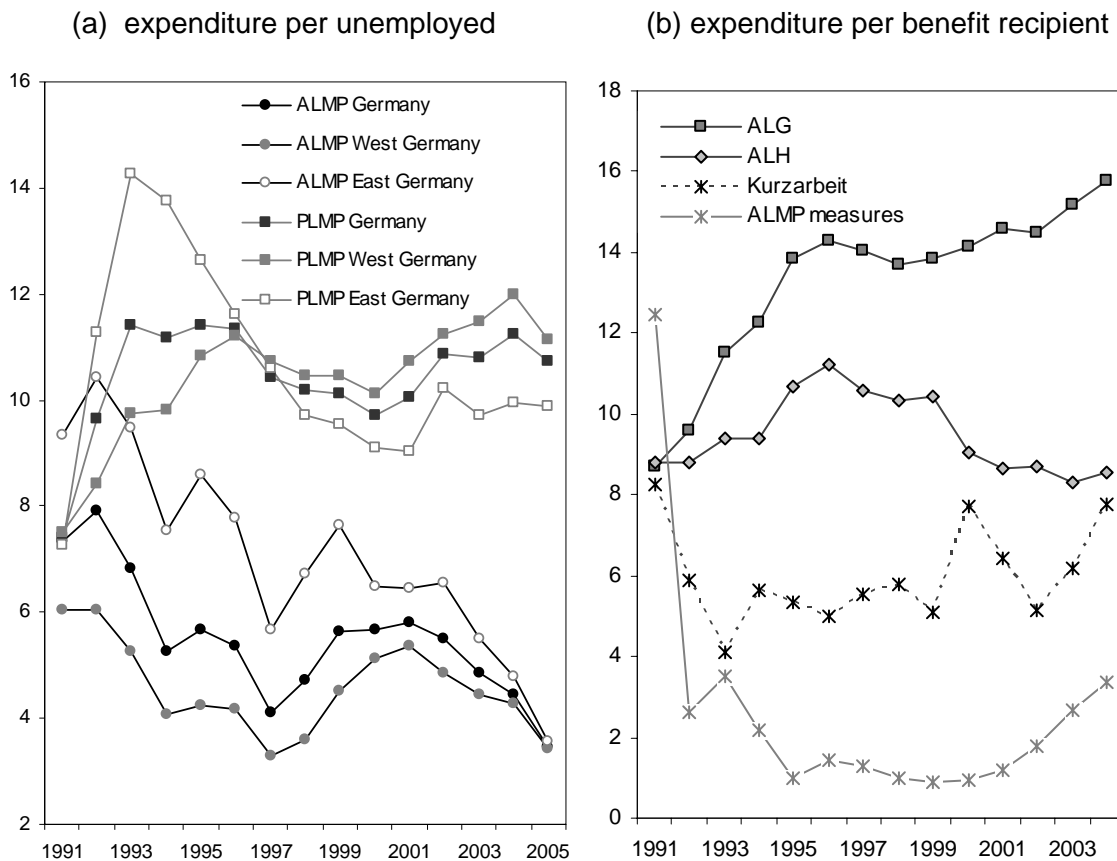
Note: (a) Federal expenditure (tax financed benefits and measures); (b) ALMP and PLMP figures do not sum up to 100% due to administrative costs.

Source: BA.

3.9 Direct Effects

Since the Federal Employment Agency (BA) is an integrated unemployment insurance and labor market administration, it finances both passive and active labor market policies through its revenues, mainly from insurance contributions. However, as shown above, the federal government finances an increasing share of the expenditures for the long-term unemployed. The distribution of funds for passive and active labor market policies has changed as a result of the increase in long-term unemployment and the limited contribution revenues available. Given that the unemployment (both insurance and assistance) benefits are right-based transfers and the state does not fund additional active labor market policies, the share of active employment promotion has declined in relation to the overall expenditures (see Figure 8).

Figure 9: Active and Passive Labor Market Policy expenditure (1,000 € per capita, Germany (West and East) 1991-2004



Notes: Active LMP, passive LMP divided by numbers of the registered unemployed; (b) by numbers of recipients, ALMP measures: job creation and training measures.

Source: BA data; Council of Economic Advisors.

Expenditures for passive labor market policies have increased mainly due to the rise in long-term unemployment, yet the average payment of unemployment assistance has decreased since the mid-1990s in West Germany and remained rather stable in East Germany, while the unemployment insurance payments increased gradually over time due to inflation and increased wages. Expenditures on passive labor market policies have followed the overall trend among an increasing number of unemployed people, particularly the long-term unemployed, which is why passive labor market expenditure per unemployed individual remained rather stagnant at 10-12,000 € (see Figure 9). While the expenditure per ALG recipient has increased rapidly in the early 1990s due to more unemployed people with longer short-term unemployment periods (below one year), it only grew gradually afterwards. The average expenditure for unemployment assistance recipients has declined since the mid-1990s.

On the other hand, active labor market expenditure has decreased despite the rising number of unemployed people, and thus active labor market policy expenditure for the average unemployed declined substantially since the 1990s, and the level converged between previously high spending in East Germany and low spending in West Germany to a generally low level. The expenditure for ALMP measures (training and job creation) have declined in the early 1990s and only recently increased again. Thus, in general there seems to be a trend that passive labor market expenditure has crowded out active labor market expenditure at a time when activation measures have grown more important. Moreover, the increased role of federal state financing due to the increased share of long-term unemployment has led to the most important reform of long-term unemployment benefits.

4 ACTIVE LABOR MARKET POLICY IN GERMANY

4.1 General and Historical Overview

Since the late 1960s, Germany has a fully fledged system of active labor market policies funded through contributions to unemployment insurance and additional state subsidies to balance the budget and finance specific target group schemes. Regarding instruments of active labor market policies, there has been a strong tendency to regulate labor market policy schemes at the national level and change them frequently while leaving significant leeway for the Public Employment Service (PES) in actual implementation of these schemes and allocating funds to different programs. The Federal Employment Office (BA) was a public body governed by tripartite self-administration (the government, employers' associations, trade unions). Regarding the overall orientation of active labor market policies, direct reintegration into the first labor market was not the first and foremost objective, but rather stabilization of individual benefit claims and incomes as well as a rather passive "buffering" of unemployment, i.e., hiding open unemployment through an expansion of placements to active labor market policy schemes such as direct job creation or extended publicly funded training. This pattern was particularly dominant after economic crises in the 1970s

and 1980s and as a reaction to employment decline in Eastern Germany after reunification. This contributed to high non-wage labor costs and raised some critique regarding the placement effectiveness of the BA and the cost efficiency of active labor market programs.

Although there had been attempts at reforming the BA and active labor market policies in the 1990s, the Hartz reforms implemented between 2002 and 2005 mark the departure from the established model of rather “passive” active labor market policy. The Hartz reforms did not only reorganize instruments, but the governance of active as well as of passive labor market policy underwent a complete overhaul in order to facilitate a more “activating” policy stance. This meant streamlining some of the instruments, stricter monitoring of costs and effectiveness and a more systematic evaluation, but also a general reorganization of the BA with the help of external consultants. After the BA restructuring, the social partners’ influence is much smaller and indirect than in the past, while management by objectives and contracting-out of services has become a more prominent feature of active labor market policies in Germany.

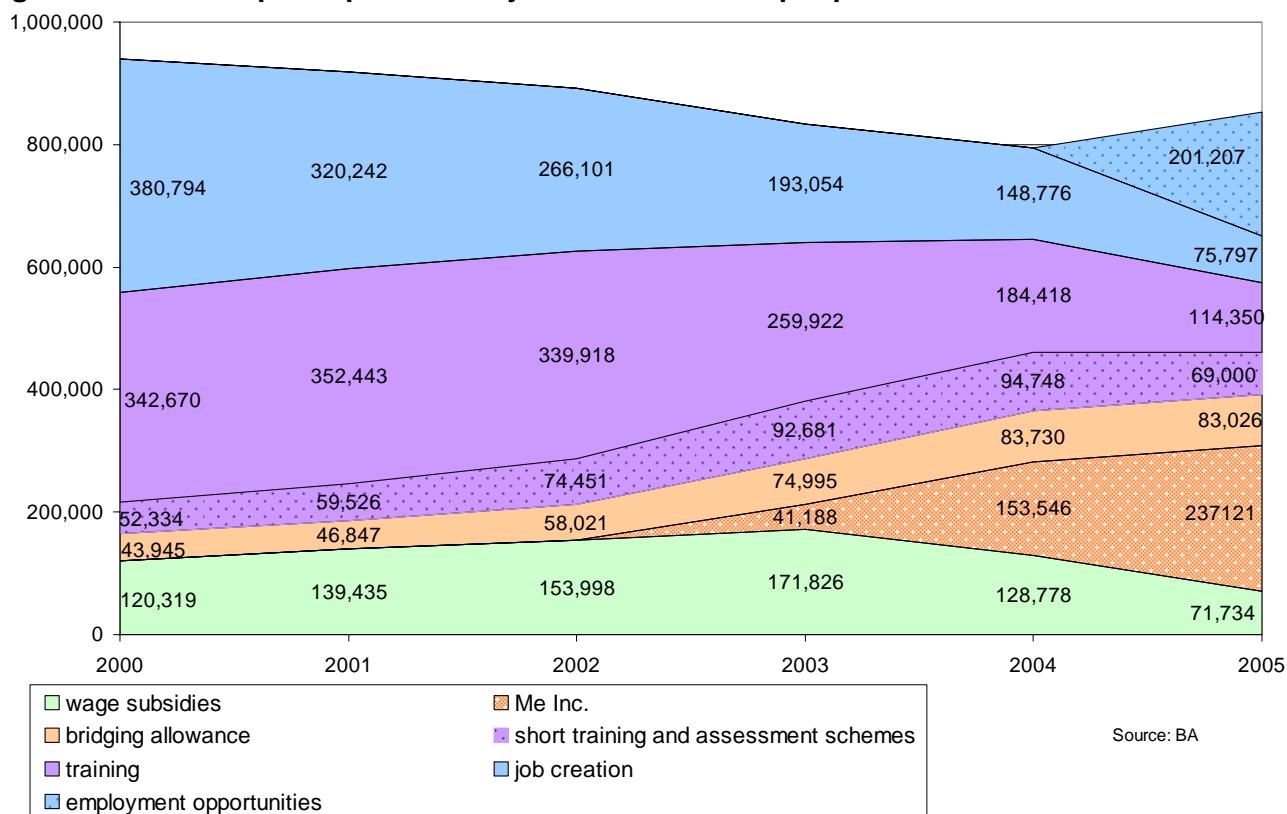
Table 7: Active labor market measures for ALG I recipients

<p>unemployment insurance (ALG I) and unemployment assistance (ALG II) recipients (SGB III)</p> <ul style="list-style-type: none"> ▪ job search assistance, monitoring, profiling, advice on vocational training ▪ job placement vouchers (since 2002) ▪ publicly funded training measures allocated via individual training vouchers (since 2003) ▪ direct public job creation schemes ▪ wage subsidies for employers in case of hiring the hard-to-place unemployed or older workers ▪ specific measures for the youth ▪ different schemes of subsidies for business start-ups: bridging allowance and Me Inc. (“Ich-AG”, under ALG II emulated by “Einstiegsgeld”) ▪ measures for the disabled (“Rehabilitation”) ▪ temporary agency work for the unemployed (“PSA”) ▪ short-time work benefits (“Kurzarbeit”) ▪ specific schemes in the construction sector aiming at continuous employment in winter ▪ specific schemes to support employment of older workers or the unemployed, such as a wage safeguard scheme, wage subsidies, and exemption of employers’ ALG contributions
<p>unemployment assistance (ALG II) recipients only (SGB II)</p> <ul style="list-style-type: none"> ▪ public employment opportunities lasting for up to six to nine months (“1 Euro-Jobs”) ▪ 12 months of a more generous earnings disregard in case of taking up a new job (Einstiegsgeld), mainly used for enterprise creation as other programs are not available under SGB II. ▪ an implicit in-work benefit through the general earnings disregard clause (“Hinzuverdienst”), which also provides an option to top up low earnings with benefit available for people without sufficient resources, i.e. Arbeitslosengeld II (“Aufstocker”).

4.2 General Description

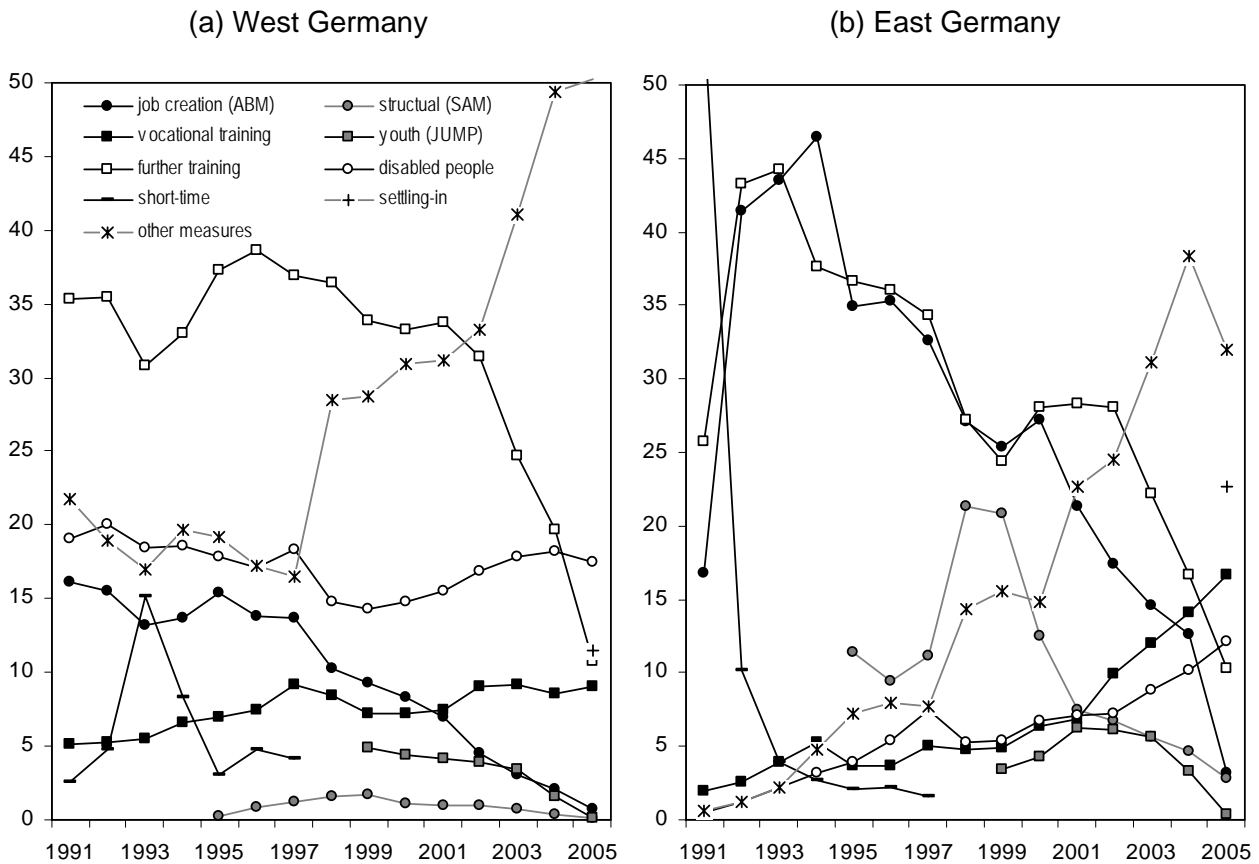
Germany now has a complex system of active labor market policies mainly regulated by federal law with the most important legislation addressing active schemes within the framework of the mostly contribution-funded unemployment insurance (the so called “Third Book” of the Social Security Act, *Sozialgesetzbuch III* or SGB III) and those tax-based programs focusing on the long-term unemployed (“Second Book” of the Social Security Act, *Sozialgesetzbuch II* or SGB II). The institutional repertoire defined by SGB III, which is available for ALG I recipients, is multifaceted and consists of the following active labor market policy schemes (see Table 7). Part-time work for older workers (*Altersteilzeit*) was originally conceived as a flexibilization of the transition to retirement and to further replacement of older workers by the young unemployed through employer subsidies, but in actual practice this has become one of the major early retirement schemes in Germany. For the long-term unemployed, i.e. recipients of ALG II, there is a similar repertoire defined by SGB II. Apart from referring to most of the programs stemming from SGB III, tax financed SGB II also allows for a more flexible and case-oriented application of activating interventions with a stronger emphasis on “in-work” benefits (see Table 7).

Figure 10: Stock of participants in major ALMP schemes pre/post Hartz



Source: BA

Figure 11: Active measures as share of Active Labor Market Policy expenditure (%), Germany (West and East) 1991-2004



Notes: Measures as % of active LMP expenditure

Source: BA data; own calculations.

Active labor market policy is financed mainly through unemployment insurance benefits (SGB III, short-term unemployed) and public taxes in so far as there may be some deficit in SGB III funding with respect to the SGB II part (long-term unemployed). Regarding the relative importance of ALMP schemes, recent data show a decline in inflow and stocks of active labor market policies in the contribution-financed framework, e.g. in publicly funded training, due to stricter criteria for the distribution of training vouchers (70% integration criteria), a decline in the use of wage subsidies, an enormous growth in inflow and stock of subsidized start-ups (bridging allowance and Me Inc.), a replacement of traditional direct job creation schemes under SGB III which were oriented at wages set by collective agreements and allowed for requalification for unemployment insurance benefits by public employment opportunities that provide 1 to 2 € per hour worked on the basis of 30 hours per week for six to nine months in addition to full benefits (“1 Euro Jobs”). The most “innovative” active labor market policy instruments addressing older workers are as rarely used as placement vouchers.

4.3 Sectoral and Firm-Level Agreements

Active labor market policies are defined at the federal level although there can be some divergence at the regional or district level, in particular in the framework of SGB II, where there is no integrated administration (see next section). However, there is no specific sectoral labor market policy in Germany except for agreements on active labor market policies for (former) employees in case of mass redundancies (*Sozialpläne*) due to major business restructuring or plant closures (*Beschäftigungsgesellschaften* or temporary work agencies). The social plan is usually an agreement between employer and works council, also there is also the possibility of a firm-level collective agreement between employer and a trade union. The agreement specifies the social criteria by which mass redundancies have to take place as well as severance pay for those set free, it is thus more a measure of partial employment protection and a passive labor market policy. However, in case where a temporary work agency is created, active labor market policies such as the job placement and re-training of redundant workers will be undertaken by the new agency. For instance, redundancies at privatized German telecom company (Telekom) were smoothed by creating a temporary work agency (Vivento) for those former employees. This agency was used for processing the first wave of ALG I claims under the Hartz IV reform. Specific provisions for active labor market schemes exist for the construction sector (*Winterbauförderung*), in particular subsidized employment.

4.4 Responsibility

There is an integrated organizational structure responsible for passive and active labor market policies for the short-term unemployed (BA), whereas responsibility for passive and active labor market policies for long-term unemployment is divided between the BA and municipalities. In most districts, joint agencies have been established (*Arbeitsgemeinschaften* or ArGe), while the municipalities have taken over these tasks in some districts (*Optionskommunen*).

The structure of active labor market policies within unemployment insurance (SGB II), but also unemployment assistance (SGB III), is basically determined by national legislation. The management of the BA and its local offices implements the ALMP (SGB III) programs. The tripartite supervisory board (*Verwaltungsrat*) supervises the BA executive board of three directors (*Vorstand*). Supervisory board members are nominated by each of the three parties. Actual implementation takes place with regional and local BA agencies. While active and passive schemes for the long-term unemployed are also defined by national legislation, local offices (ArGe and *Optionskommunen*) carry them out. Due to higher flexibility in legislation on activation programs for the long-term unemployed, there is more leeway in actual implementation. In contrast to SGB III labor market policies, there is no unified responsibility but joint governance by BA and municipalities, while federal and municipal tax revenues share expenditure.

Hence, this policy area is currently characterized by major governance problems due to a lack of a clear distribution of responsibilities and ambiguous incentives for implementing actors. The BA focuses its own activities in active labor market policies (funded by unemployment insurance con-

tributions) on better risks, i.e. the potentially short-term unemployed, whereas the potentially long-term unemployed identified through profiling are neither provided with enabling active labor market schemes nor subject to “demanding” or activating elements during the period that they draw unemployment insurance benefits. Thus, the profiling’s expectation of individuals becoming long-term unemployed is a self-fulfilling prophecy. After expiry of ALG I, the long-term unemployed are transferred to tax-financed *ArGe* and *Optionskommunen*. The federal government then pays benefits, and reintegration into the regular labor market is more difficult the longer unemployment lasts (Eichhorst/Schneider/Zimmermann 2006). Hence, there are new “Verschiebebahnhöfe” (literally: switching stations) between the different schemes for the short- and long-term unemployed, although the original aim of the reform was to establish a unified framework with one-stop shops for all jobseekers. Expenditure on unemployment insurance benefits and active labor market policies for the short-term unemployed tend to decline at the expense of higher expenditure on tax-based unemployment assistance and active labor market programs for recipients of unemployment assistance. This means a shift towards a tax-financed labor market policy. This emphasis on cost/benefit relations by the BA management is in stark contrast to the situation before the Hartz reforms were implemented. Regarding the costs and benefits of assigning the unemployed to ALMP schemes as opposed to benefit receipts, there had not been an explicit calculation of the cost efficiency in the past. This was first introduced with the Hartz package that resulted in a complete overhaul of the BA’s internal management and controlling. Applying stricter effectiveness and efficiency criteria in ALMP – in particular in active schemes for ALG I recipients that are administered by the BA – is also responsible for the relative decline of expenditure and participation in ALMP.

Regarding the evaluation of the employment effects of ALMP schemes in Germany, there has traditionally been a neglect of systematic analysis before the Hartz reforms. However, research into the effectiveness of selected ALMP schemes carried out in the pre-Hartz period justified a skeptical assessment of ALMP (Caliendo/Steiner 2005, Schmidt et. al. 2001, Konle-Seidl 2005), especially regarding the placement effects of publicly sponsored training and direct job creation schemes. These results created a general reluctance with respect to future continuation of traditional ALMP. With the Hartz reforms bringing about a complete overhaul of the institutional repertoire of ALMP in Germany, they also triggered a comprehensive macro- and microeconomic evaluation exercise concerning the reorganization of the PES and ALMP within the framework of unemployment insurance (SGB III). Interim reports were presented in early 2006, and final reports will become available in early 2007. Some of the evaluation studies available at this point, however, suffer from short observation periods (Bundesregierung 2006, Jacobi/Kluve 2006, Kaltenborn et al. 2006, and the contributions to Caliendo/Steiner 2006). Evaluation of the Hartz IV reform, i.e., the shift towards activation of the long-term unemployed (SGB II), is still in progress with first results to be expected in 2008.

Table 8: Overview of Hartz evaluation studies

Instrument	Effect	Comments
Publicly funded training	Positive	Reduced lock-in effect compared to older and longer measures, better employment perspectives after training; long-term effects still unclear
Wage subsidies for employers	Positive	Effects on accelerated exit from unemployment and return to non-subsidized employment compared to non-subsidized jobs, but high windfall gains and associated costs
Enterprise creation	Positive	Some reduction of unemployment, but most participants observed still in subsidization period, considerable windfall gains and costs
mini-jobs and midi-jobs	Positive	Creation of additional marginal jobs after recent reform – but potential displacement of regular employment, no bridge to part-time or full-time work
Direct job creation	(Negative)	Delayed return to regular employment
Measures for older workers	No effect	No effects identifiable
Temporary agency work for the unemployed (PSA)	Negative	Delayed return to regular employment due to lock-in effect
Liberalization of commercial TWA	Positive	Additional job creation in TWA firms
Placement vouchers and contracting-out	No effect	No effects of using private placement agencies identifiable
Contracting-out of other integration services	Positive	Better chances to return to employment in comparison with the unemployed not benefiting from private providers

Source: authors' compilation based on Bundesregierung 2006, Kaltenborn et al. 2006 and contributions to Caliendo/Steiner 2006.

The influence of social partners was reduced significantly in the context of the Hartz reforms as they had been criticized for not being interested in an efficient allocation of funds and rather subsidizing training providers associated with either the trade unions or the employers' associations. More broadly speaking, the Hartz report made tripartism in operative decisions responsible for ineffective and bureaucratic work of the BA. Hence, after the reforms, the management of the BA had been strengthened and is more autonomous now. While a general privatization of the BA, was not considered seriously, performance of the BA in job placement was to be improved through more intense competition with private providers of placement and contracting-out of some services. Private job placement had been liberalized in the mid-1990s but did not play a major role so far. Quasi-market mechanisms became only more important in active labor market policy with the Hartz reforms, i.e. contracting-out of services using competitive tendering for services provided by external companies and for the use of training and placement vouchers that introduce more intense competition into the field of job placement. This led to the erosion of traditional close networks between PES and providers of training and other services that were often affiliated with the social partners. In the old system before Hartz, social partners involved in the implementation of active labor market policies could allocate resources to service providers under their control (with little transparency and supervision of quality and appropriateness of the services provided).

Table 9: Before and after Hartz Organizational Reforms of the BA

	Before Hartz Reforms	After Hartz Reforms
Executive board	President, appointed by federal government; Head of public administration	Executive Board (3 members, one chair), nominated for 5 years (renewal possible) by supervisory board and appointed by federal government; Chair: central steering and IAB research Co-chair: staff and finances Co-chair: operative policies (products and programs), SGB II
Supervisory board (Verwaltungsrat)	51 members tripartite: employers, trade unions, state (Bund, Länder, communes)	21 members tripartite: employers, trade unions, state (Bund, Länder, communes) supervision of board, can fire executive board members (upon approval of federal ministry)
Administration	Departments: <ul style="list-style-type: none"> ▪ labor exchange and advise ▪ pre-occupational training ▪ transfer payments ▪ internal administration „Arbeitsamt 2000“ Reform: mixed, multi-departmental teams	Centers: Functional centers <ul style="list-style-type: none"> ▪ steering of regional directorates ▪ controlling and finances ▪ products and programmes internal services and IAB research institute regional directorates: matrix organization
Organizational levels	Federal office (BA) 11 Landesarbeitsämter 184 Arbeitsämter 650 subdivisions plus special departments	Federal agency headquarter (BA) 10 regional directorates 178 agencies, 660 offices BA supervises regional directorates which controls agencies
Management	decrees (Erlässe) by departments of BA or order (Verfügungen) of Landesarbeitsämter	management by objectives (Zielvereinbarung)
Controlling	no in-house controlling, only labor market statistics	since 1998: internal controlling at BA head- quarters
Employment policies	monopoly of BA (Beschäftigungsförderungsgesetz BeschFG 1994)	<ul style="list-style-type: none"> • right to private job placement (voucher after 6 weeks) • Temp-agencies as job placement offices (PersonalServiceAgenturen (PSA)) • Retraining vouchers (Bildungsgutscheine)

Source: Bieber et al. 2006.

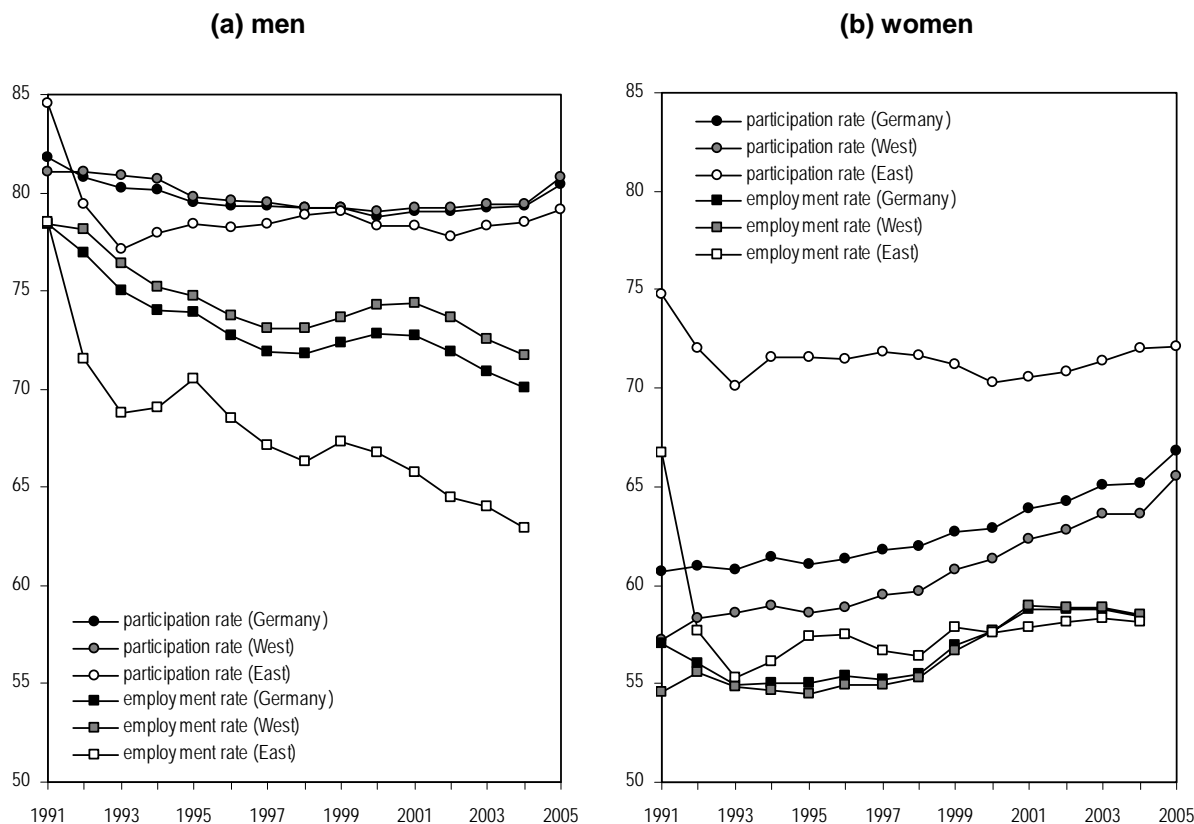
5 EMPLOYMENT PERFORMANCE

In order to evaluate the performance of German labor market institutions, one needs to take into account that the German labor market had to deal with a special situation after unification in 1990. The transition of the East German planned economy to a market economy has been an unprecedented challenge. The restructuring of East German production and services from a state-run to a market economy led to a decline in employment by 20% over the last fifteen years, whereas the labor force remained stagnant in the West despite population migration from East to West Germany during the 1990s. Unemployment increased in East Germany from 1.0 million in 1991 to 1.6 Mio in 2004, though it also climbed from 1.6 to 2.8 million in West Germany. The unemployment rate in the East is twice as high as that of the West German labor market. The transition occurred largely by adopting the West German institutions of employment protection, social insurance and labor market policies to a new, more polarized situation. While there had been problems with West Germany before 1990, the bad employment performance and unemployment problems deteriorated even further since unification, as most institutional arrangements remained inert and were transposed to the East German economy. Moreover, a large share of the costs of unification was shouldered by the West German social insurance schemes, including unemployment insurance, increasing (non-wage) labor costs even further. At a time when West Germany had decided to reduce passive labor market policies, the expenditure for such policies increased under the aggravating labor market situation in East Germany.

5.1 Labor Market Participation

Germany's labor force participation rate has been much lower than in liberal market economies (USA, UK) or in the Nordic economies due to lower female labor force participation and early exit from work (Ebbinghaus 2006). The participation rate among men constantly remained at 80% since the early 1990s, while it is somewhat higher in Nordic countries or increased in countries with employment growth like the Netherlands and Ireland over the last ten years. Although female labor force participation has increased to currently 66% since unification, the overall rate is still below the Nordic countries. There are, however, significant differences between East and West Germany. Female labor force participation was already much higher in the GDR and continued, after a slight drop, to be high after unification (above 70%), despite increased unemployment and massive early retirement among older women. The lower participation of women in West Germany (below 60% during the 1990s and increasing to 66% in 2005) is due to the limited access to childcare, particularly for children under the age of three, and for all-day kindergarten and primary schools. Moreover, part-time work is, therefore, more common among West German employed women (45% in 2004) than among East German employed women (28% in 2004). Due to the higher participation of women in the East German labor market, the overall rate of participation is higher than in West Germany.

Figure 12: Participation and employment rate for men and women (%), Germany 1990-2005



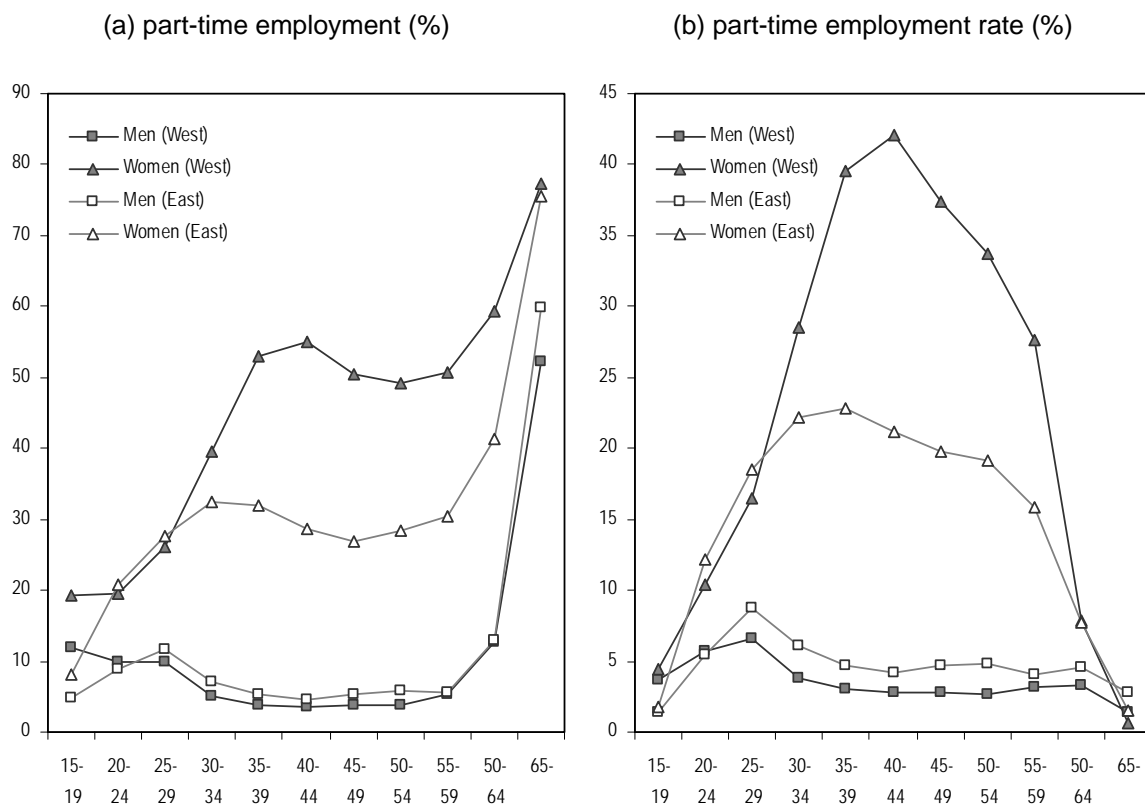
Notes: Participation rate: employed and unemployed in % of working-age population (aged 15-64); employment rate: employed (ILO-definition) in % of working-age population (aged 15-64).

Source: Mikrozensus 1991-2005; Statistisches Bundesamt and BA.

Due to unification, the German labor force grew by more than eight million from 32 to 40 million people working or seeking employment. Due to immigration, the labor force of foreign workers increased by one million during the early 1990s, though not counting the large inflow of about 200,000 ethnic Germans from Eastern Europe (*Aussiedler*) per year in the early 1990s. In addition to the labor force of about 43 to 44 million, the “silent reserve”, those being on training measures or seeking work in the near future, added nearly 2.2 million during the 1990s, though with declining tendency (1.5 million in 2005) due to the cut in training measures from 1.4 million in 1995 to 0.7 million in 2005.

5.2 Full and Part-time Employment

The employment rate provides an indicator of the degree of gainful employment of a society. Germany’s employment rate remains below the EU target of 70% by 2010, due to high unemployment, lower female participation rate and early retirement. One major East-West divide has been the opposing development of gainful employment: the employment rate declined slightly in East

Figure 13: Part-time employment by age group, West and East Germany 2004

Notes: (a) Part-time employees in % of dependent employment; (b) part-time employment rate in % working population aged 15-64.

Source: Mikrozensus 2004; own calculations.

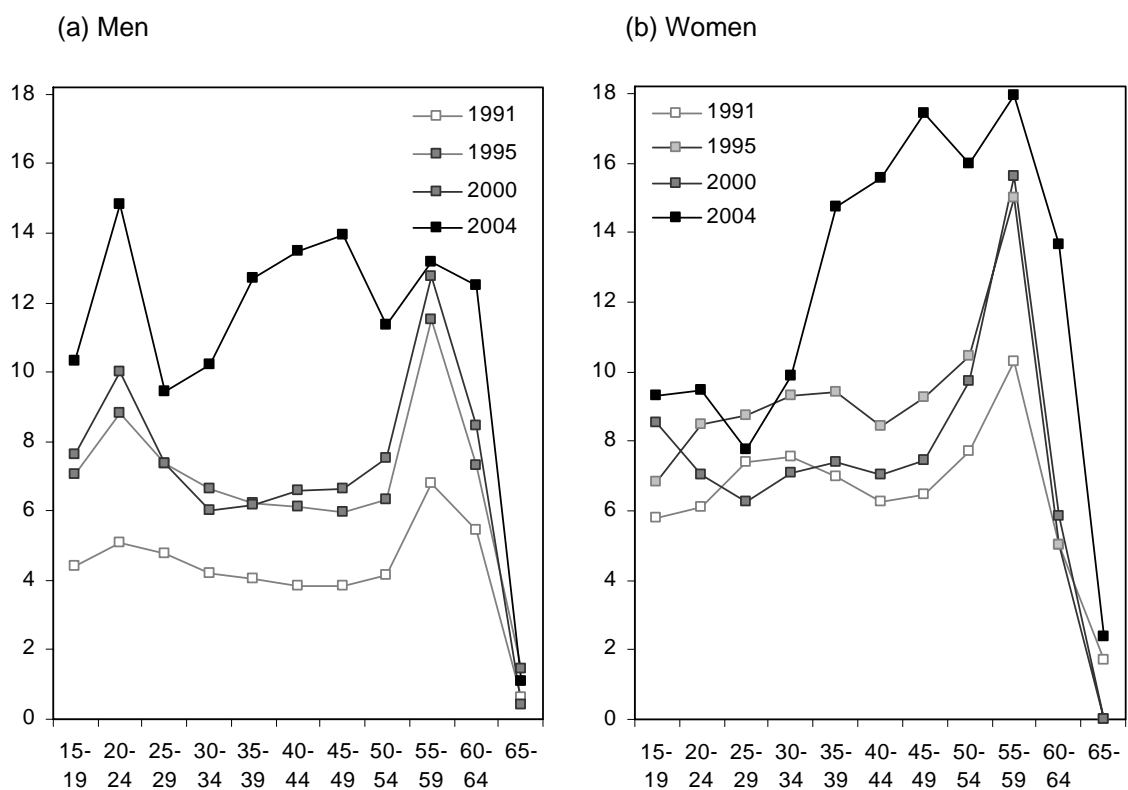
Germany from over 65% in the early 1990s to below 62%, while it increased slightly in West Germany. While the overall employment rate shows only slight changes, the level of gainful employment differs considerably between men and women. The West German employment rate among men declined slowly during the early 1990s and again in the early 2000s, while employment receded more rapidly and steadily after a massive drop immediately after unification. The employment rate for women is relatively similar in East and West Germany, despite the much higher participation rate of women in the East. East German women also suffered from a massive decline of more than ten percentage points in the early 1990s and have only gradually regained a few percentage points.

One form of flexible employment is part-time employment, often half working week contracts around 19-20 hours with the same social insurance contribution rate as full-time contracts. Part-time employment (excluding mini-jobs) remained relatively infrequent before unification; only 4% of the dependently employed were working part-time in the 1960s, increasing to 12% in the mid-1970s. Part-time employment increased from 16% in 1995 to 24% in 2005, yet it remained a phenomenon mainly among women (44% of employees worked part-time in 2005) and rarely among

men (7%). For women, the share of part-time work increases with age until around age 40-45 in West Germany and age 35-39 in East Germany. Thereafter it declines slightly until age 55 when it again increases due to partial retirement. Women with children partially withdraw from employment in order to balance childcare responsibilities and work, given the low availability of all-day childcare facilities and primary school services. Yet there is also a significant regional divide in both the share of part-time in overall dependent employment as well as in the employment rate of part-time employees. The part-time employment rate (part-time employment in percent of the respective population of the age group) among mid-career women in West Germany is about twice as high as in the East. Thus, among the 40-45-year-old women, 42% work part-time in the West compared with 22% in the same age group in the East, while the full-time employment rate is much higher among East German women.

With the exception of young men, who are twice as likely to work part-time due to combining work and higher or vocational education, there is no particular age-related part-time pattern among men until age 60. Part-time employment in the age group 60-64 is used as a partial early retirement option and from 65 onwards as a way to combine income from pension and work, though, given the low employment rate, these are only few older men.

Figure 14: Unemployment rate (ILO) by age group and gender (%), Germany 1990-2004



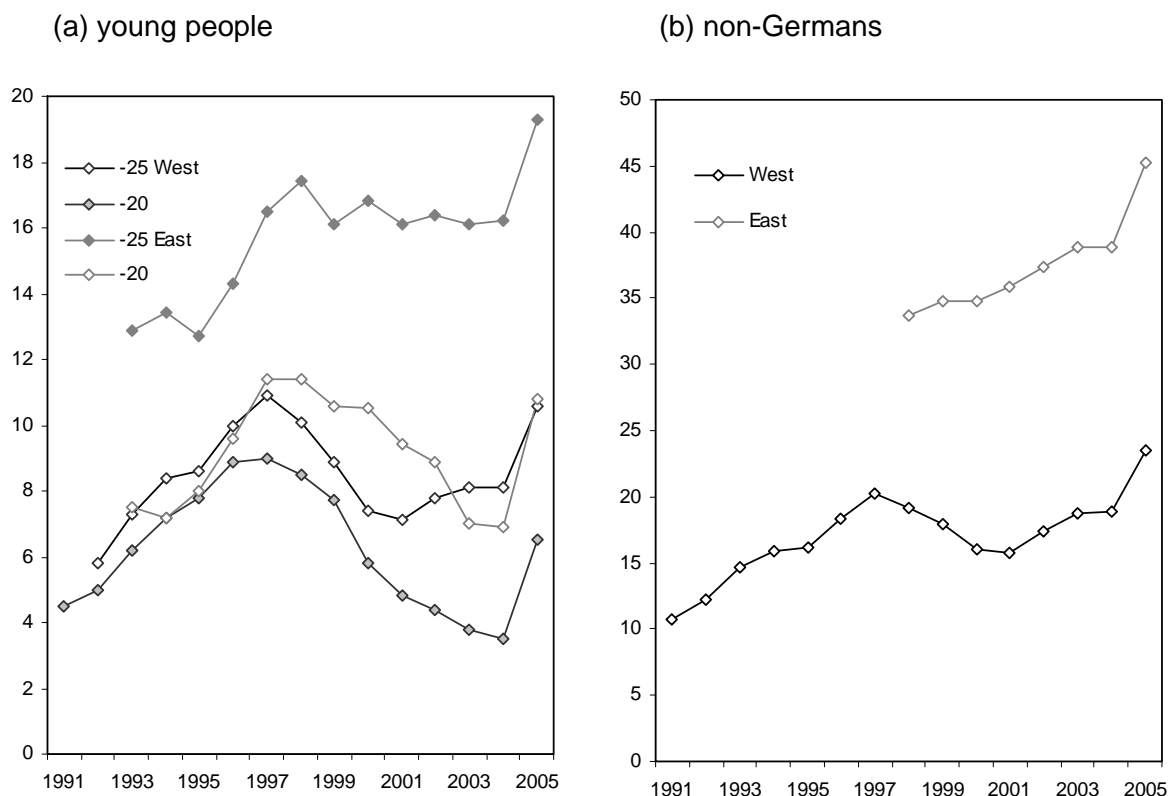
Notes: Unemployment rate (ILO definition) in % of age group.

Source: OECD Labor Force Statistics (based on micro-censuses 1991-2004); own calculations

5.3 Unemployment Risk Groups

While the registered unemployment rate was higher for women than for men in West Germany during the 1980s (see Figure 1), the gender difference became very small during the 1990s, and the female rate turned even somewhat lower during the early 2000s. After unification, however, the registered unemployment rates in East Germany increased more rapidly for women during the early 1990s and stayed at a higher level than for East German men, though they caught up in the late 1990s and have surpassed women since 2004. Unemployment has increased across all age groups since the early 1990s for both men and women in Germany. Unemployment rates were already higher in the early 1990s and then increased among the older workers (55+) as those were increasingly pushed out of work by structural adjustments and long-term unemployment benefits that provided a bridge to early retirement. With increased unemployment in recent years, unemployment became widespread across all age groups above 35 years for both men and even more so for women. Long-term unemployment has become widespread, particularly in East Germany. Given the large differences in unemployment levels between the lower level in the West and the higher level in East Germany, unemployment also affected the different groups somewhat differently.

Figure 15: Unemployment rate of young people and non-Germans (%), West and East Germany 1991-2005



Notes: BA registered unemployed in % of dependently employed of same age group; -20: under 20 years old; -25: under 25 years old; non-Germans: alien residents, excluding Aussiedler.

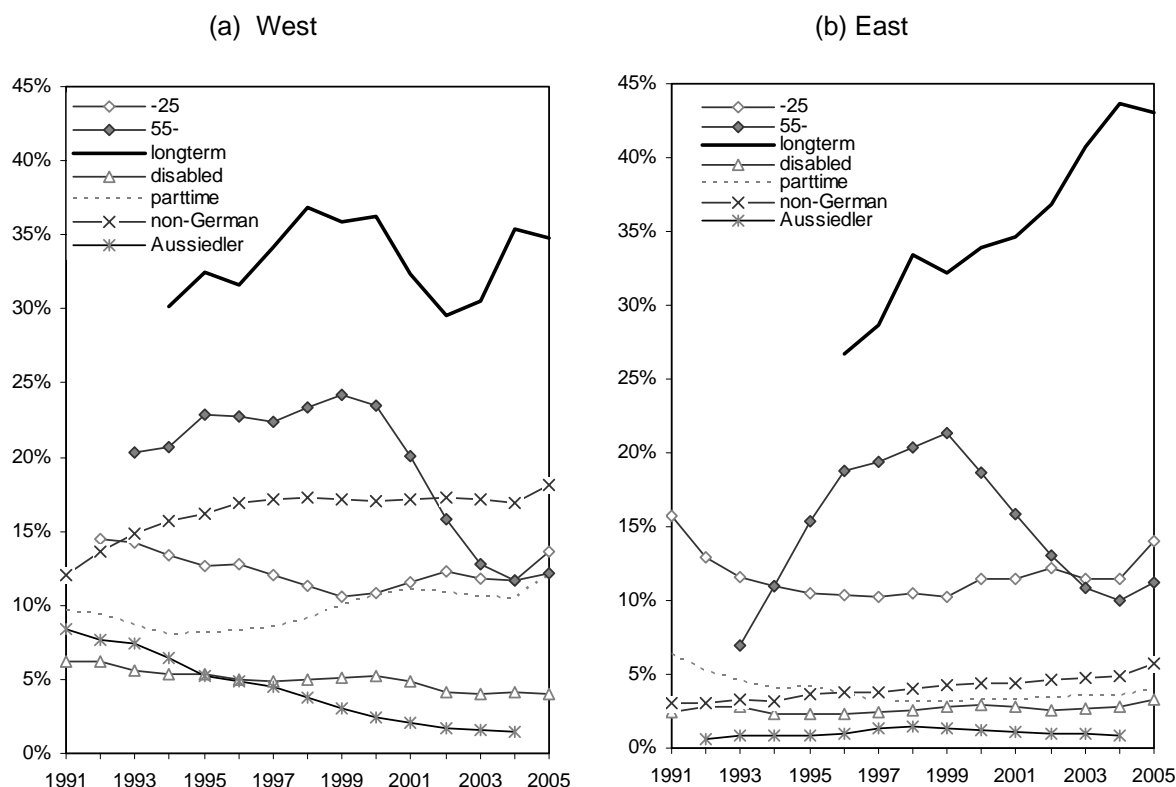
Source: BA database 2006; own calculations

Although the German dual vocational training regime has performed well with relatively low youth unemployment rates over several decades in comparison to most other European countries, unemployment increased particularly rapidly among the very young (see Figure 15). There are major difficulties with vocational training today as the supply of such positions fails to meet demand on the one hand, and some school leavers lack basic qualifications on the other hand. Despite the fact that government-initiated training substitute programs and other ALMP measures addressing the young have been expanded over the last decade, youth unemployment increased during the late 1990s and more recently due to the Hartz reform activation of all assistant claimants in a household). Unemployment among men aged 20-24 grew particularly rapidly as the school leavers found no vocational training or subsequent job, while unemployment among younger women was less common.

Non-Germans, i.e. immigrants of the first or a subsequent generation, mostly concentrated in industrialized West Germany due to the inflow before the immigration stop in the 1970s, are particularly frequently exposed to unemployment (see Figure 16). The registered unemployment rate for non-Germans more than doubled from 10.7% in 1991 to 23.5% in 2005, while the rate is twice as high (45% in 2005) among the few non-Germans in the East (only 3.5% of the non-German labor force live in the East). Although the employment rate is somewhat higher among the non-Germans, the unemployment risk is particularly high for non-Germans (17% in West Germany and 33% in East Germany) but also for dual citizens (15%/39%) other than from western EU member states (7%/22%), in particular those from eastern Europe (18%/ 37%), Ex-Yugoslavia (15%/37%), from Turkey (23%/39%) and from other parts of the world (21%/33%) (Mikrozensus 2004). The high unemployment risk indicates the combination of several risk factors: higher rate of dropouts, lower level of formal education and vocational qualification and language skills, larger share of young people seeking training or employment, concentration in industrial jobs for older workers.

After the disintegration of the communist Eastern Bloc, ethnic-Germans (*Aussiedler*) from Eastern Europe migrated at large numbers to Germany (200,000 per year during the early 1990s), being attracted by German citizenship status and the possibility to flee the economic and political situation in their home countries. While the first migrant groups had better German knowledge, later groups tended to be less fluent with higher unemployment risks. Nevertheless, the share of ethnic-Germans mainly migrating to economically more prosperous West Germany has decreased since the early 1990s, indicating their long-term integration into the German labor market.

Figure 16: Share of particular groups among the BA registered unemployed (%), West and East Germany 1991-2005



Notes: BA registered unemployed by group (% total): youth under 25 years, older workers 55+ years, long-term unemployed (one year and more); disabled (Schwerbehindert); part-time: seeking part-time employment; non-Germans (no German citizenship); Aussiedler (ethnic-Germans from Eastern Europe, granted German citizenship).

Source: BA database 2006; own calculations

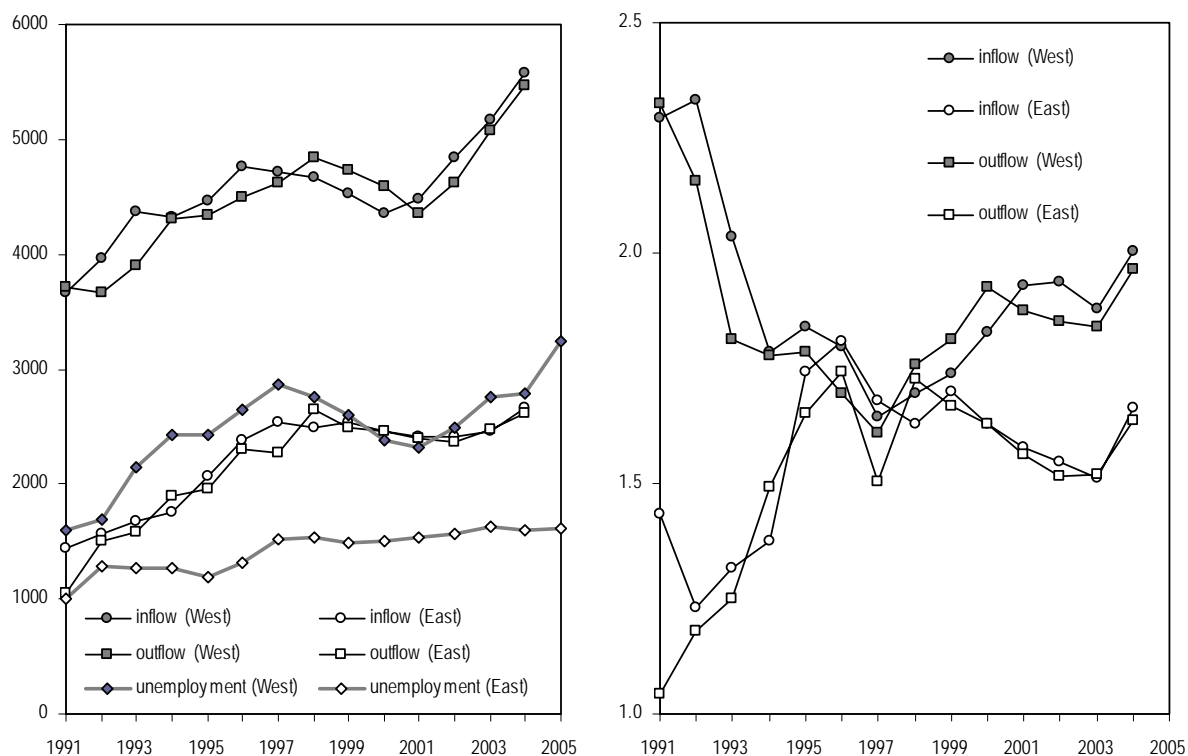
5.4 In and out of Unemployment

Long-term unemployment has been relatively high in Germany. According to the OECD indicators, about half of all the unemployed have been without a job for more than one year during the 1990s and 2000s. The share of long-term unemployment among the BA registered unemployed is somewhat lower due to the administrative practice of ending unemployment spells due to training measures or early retirement. Nevertheless, even among the BA registered unemployed the numbers of the long-term unemployed above one year have increased in times of economic downturn in West Germany and increased on a long-term base in East Germany from below 25% in the early 1990s to above 50% in 2000s.

Figure 17: Inflow into and outflow of unemployment, Germany 2004

(a) inflows, outflows and unemployment (1000s)

(b) inflows or outflows per unemployed



Notes: (a) Inflows and outflows of BA registered unemployment and (b) inflows or outflows divided by unemployment.

The increasing share of long-term unemployment (12 months and more) indicates the particular situation of jobseekers with persistent problems to find employment. However, a large share of jobseekers remains unemployed for a relatively short period. According to the self-reported length of job-seeking (including, besides the unemployed, job-seekers who are currently employed or inactive), there is an increasing share of unemployed in the bracket below 12 months, and a major drop in the share thereafter when most of the unemployed have to claim unemployment assistance (today ALG II). The pattern in East Germany differs from the West German one in the lower share of the unemployed with shorter unemployment spells than one year and in the share of very long unemployment (above two years). The survival curve in Figure 18.b also indicates that the West German unemployed do exit earlier than East Germans, and that the chances to exit early have decreased in East Germany over the eight years from 1996 to 2004.

Table 10: Inflows into unemployment 2004

	Germany		West		East	
	(1000s)	%	(1000s)	%	(1000s)	%
Total inflows	8,179.3	100.0	5,535.6	100.0	2,643.7	100.0
Employment (without training)	4,216.5	51.6	2,855.7	51.6	1,360.8	51.5
Employment on first labor market	3,797.7	46.4	2,671.8	48.3	1,125.9	42.6
Employment on second labor market	178.3	2.2	26.8	0.5	151.5	5.7
Job creation / structural adjustment	174.7	2.1	26.7	0.5	148.0	5.6
Job creation infra-structure measures	3.6	0.0	0.1	0.0	3.5	0.1
Self-employed / Family Workers	146.5	1.8	104.2	1.9	42.3	1.6
Other Employment (not specified)	94.1	1.2	52.9	1.0	41.2	1.6
Education / Training	1,116.9	13.7	688.1	12.4	428.8	16.2
in-firm/external vocational training	392.2	4.8	266.4	4.8	125.8	4.8
job-related training (FbW)	16.2	0.2	10.9	0.2	5.4	0.2
Integration of disabled persons	3.2	0.0	2.5	0.0	0.7	0.0
vocational preparation measures	0.3	0.0	0.1	0.0	0.2	0.0
secondary or tertiary education	724.7	8.9	421.7	7.6	303.0	11.5
job-related training (FbW)	123.0	1.5	67.5	1.2	55.5	2.1
Integration of disabled persons	18.7	0.2	11.8	0.2	6.8	0.3
vocational preparation measures	1.7	0.0	0.8	0.0	1.0	0.0
Training (not specified)	*		0.0	0.0	*	
Non-employment (without training)	2,838.5	34.7	1,986.6	35.9	851.9	32.2
disability	1,041.6	12.7	647.7	11.7	394.0	14.9
renewed after failed registration	260.5	3.2	190.5	3.4	70.0	2.6
registered by social assistance office	227.4	2.8	162.6	2.9	64.9	2.5
others (once already employed)	1,041.9	12.7	785.9	14.2	256.1	9.7
others (never employed before)	267.0	3.3	200.1	3.6	66.9	2.5
inactivity (not specified)	5.0	0.1	*		3.0	0.1
Unknown	7.3	0.1	5.2	0.1	2.2	0.1

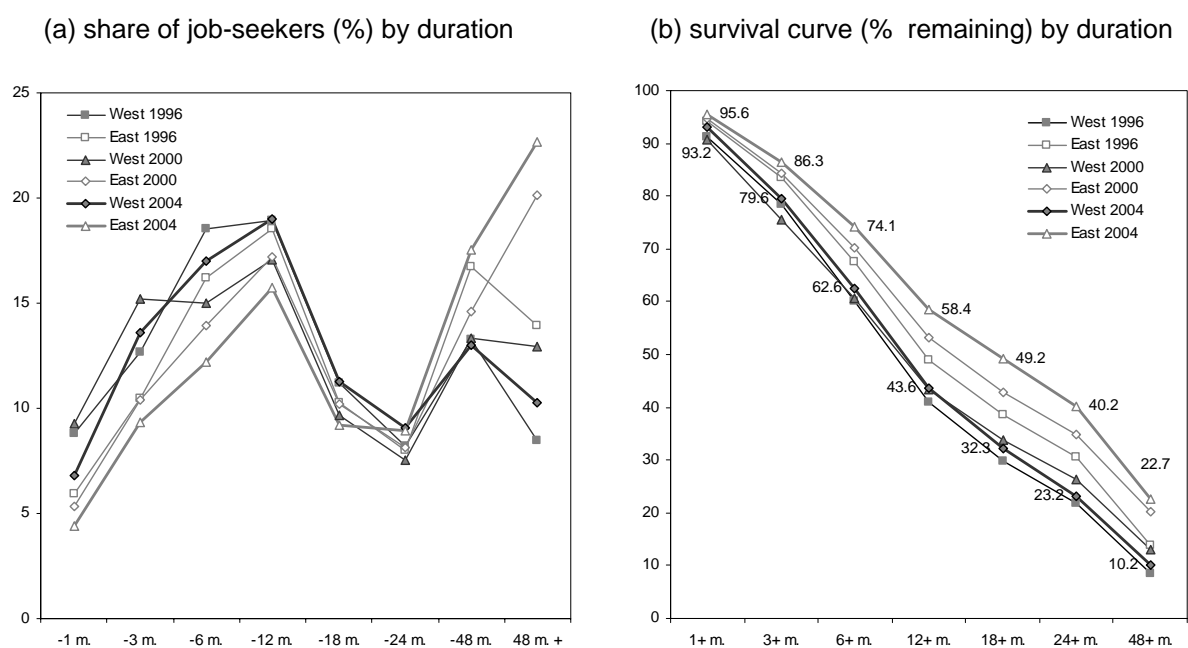
BA Arbeitsmarktstatistik 2004

Table 11: Outflows from unemployment 2004

	Germany		West-Germany		East-Germany	
	(1000s)	%	(1000s)	%	(1000s)	%
Total outflows	8,030.1	100.0	5,425.6	100.0	2,604.5	100.0
Employment	3,106.4	38.7	2,044.9	37.7	1,061.5	40.8
Dependent Employment	2,709.5	33.7	1,772.7	32.7	936.8	36.0
placement through BA	496.5	6.2	261.0	4.8	235.5	9.0
reemployment by same employer	557.6	6.9	357.5	6.6	200.1	7.7
placement thru external agencies	70.3	0.9	30.6	0.6	39.7	1.5
employer search in AIS	2.8	0.0	1.9	0.0	0.9	0.0
employees own job search	1,582.2	19.7	1,121.7	20.7	460.5	17.7
Labor Market Integration	164.6	2.0	95.9	1.8	68.7	2.6
Personnel Service Agencies	51.9	0.6	34.8	0.6	17.1	0.7
Settling-in benefits	91.5	1.1	48.5	0.9	43.0	1.7
Start-up subsidies	12.7	0.2	7.2	0.1	5.5	0.2
Second Labor Market	123.6	1.5	26.6	0.5	97.0	3.7
Job creation schemes (ABM)	120.5	1.5	26.6	0.5	93.9	3.6
Employment	396.9	4.9	272.3	5.0	124.7	4.8
Self-Employed	347.8	4.3	244.6	4.5	103.2	4.0
with bridging allowances	122.9	1.5	91.6	1.7	31.4	1.2
with self-emp. grants (start-up)	128.8	1.6	87.5	1.6	41.3	1.6
Military-/Civilian Service	49.1	0.6	27.7	0.5	21.5	0.8
Training / qualification	1,361.2	17.0	910.8	16.8	450.5	17.3
secondary or tertiary education	167.7	2.1	116.9	2.2	50.8	2.0
vocational or other training	46.2	0.6	31.4	0.6	14.7	0.6
FbW / German language courses	189.3	2.4	128.6	2.4	60.7	2.3
Training measures	958.1	11.9	633.8	11.7	324.3	12.5
Other non-employment	2,868.8	35.7	2,017.1	37.2	851.7	32.7
disability	1,273.7	15.9	818.6	15.1	455.1	17.5
moving to another BA-area	47.2	0.6	32.4	0.6	14.8	0.6
retirement	62.6	0.8	42.7	0.8	19.8	0.8
special regulations (§ 428 SGB III)	178.7	2.2	123.3	2.3	55.3	2.1
failure to renew registration*	635.3	7.9	463.7	8.5	171.6	6.6
failed availability/cooperation*	671.3	8.4	536.3	9.9	135.0	5.2
Other reasons (without verification)	693.7	8.6	452.8	8.3	240.9	9.2

Source: BA Arbeitsmarktstatistik 2004

Figure 18: Duration of job search by months, Germany 1996, 2000, 2004



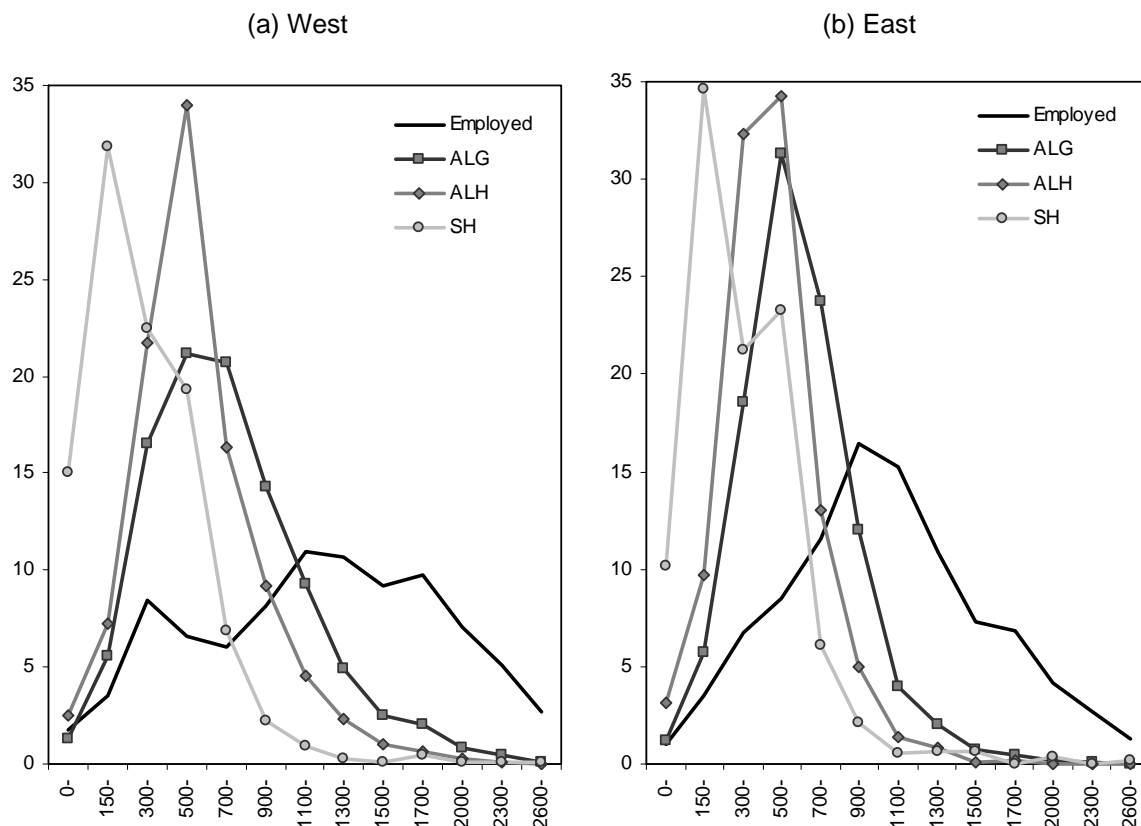
Notes: (a) jobseekers by duration (in months), (b) jobseekers remaining by duration (in months) calculated by cross-sectional analysis.

Source: Mikrozensus 1996, 2000, 2004; own analysis and calculations.

The institutional design of unemployment benefits also affects the duration of unemployment. The share of those seeking employment declines after the twelve-month-period when the transition from unemployment insurance to unemployment assistance benefits occurs (Figure 18.a). Among the unemployed, the groups under 12 months are relatively frequent, as are the groups over 48 months, where the unemployed in the West tend to have searched for a shorter time than those in the East. In particular, the group of the long-term unemployed over 24 months is much larger in East Germany, with an increasing tendency. The cross-sectional survival curve in Figure 18.b also shows some West-East differences: 20% of the unemployed in West Germany have been searching for less than 6 months, while less than 45% in the West are unemployed for over a year, but nearly 60% in the East are. Over time, the share of those with longer unemployment spells has increased in East Germany. Thus, long-term employment has become an increasing trap for people in East Germany, while it remains less dominant in West Germany.

An analysis of the impact on income due to unemployment can be partly derived from Figure 19 on the distribution of monthly individual income of different transfer groups compared to the employed. The income distribution for the employed in West Germany is somewhat wider spread and shows two peaks, one at the medium level of income and one at a very low level congruent with that of unemployment benefits. In East Germany, the income distribution is more pointed at a peak around 1000 € per month. The unemployment insurance benefits are more widespread and

Figure 19: Distribution of individual net monthly income among the employed and transfer recipients (%), Germany 2004



Notes: distribution of individual monthly income (in €) from all sources by main income source (%): employment (*Erwerbstätige*), transfer recipients: ALG (*Arbeitslosengeld*: unemployment insurance), ALH (*Arbeitslosenhilfe*: unemployment assistance), SH (*Sozialhilfe*: social assistance). Resident working population 15-64.

Source: Mikrozensus 2004; own calculations

higher than the other types of benefits, given the higher net replacement rate and the close relationship with former income. Unemployment assistance is often lower and more concentrated (ALH) given the lower replacement rate and the link to former income (before the Hartz reform). Social assistance transfers are concentrated at a much lower level, although they vary with family situation.

6 CONCLUSION

In general terms, the German system of protection against employment risks is a system with only a minor resemblance to an insurance market. This holds for both employment protection and unemployment benefits where the basic features are defined by law. In that sense, government and parliament are crucial for shaping the system, following more a political logic of office-seeking and vote maximization. Almost all employees are covered by legal employment protection: dismissal protection in case of open-ended contracts or relative stability of fixed-term employment. Simi-

larly, unemployment insurance and basic income schemes are regulated through general legislation. Unemployment insurance is funded through compulsory social insurance contributions, while unemployment assistance is funded by general taxes. There is no room for individual choice or voluntary insurance except for the recent opting-in option for the self-employed with prior employee status.

Market mechanisms, however, play a role to the extent that the use of different types of employment contracts, i.e. open-ended vs. fixed-term employment or regular part-time vs. marginal jobs, is influenced by employers' demands for flexibility and lower labor costs. The role of social partners is largely limited to bargaining. There are collective agreements on additional employment protection through sectoral or enterprise-level agreements, in particular regarding stronger dismissal protection in case of longer tenure and with respect to severance pay and reemployment aids in case of mass redundancies. Private actors have become more prominent as contracting-out of active labor market policy services has grown over the last decade, most significantly in the area of job placement and training. Vouchers distributed to the unemployed establish a quasi-market for placement and training services. The public employment service can also contract-out other services deemed necessary for accelerated reemployment.

The three mechanisms of protection against labor market risks – employment protection as well as the active and passive labor market policies in Germany are characterized by the following trends. First, a partial liberalization of rather restrictive employment protection at the margin; as a consequence, employment growth is concentrated in the flexible labor market segment; hence, the German labor market is highly segmented with persistent long-term unemployment and low labor market integration of more vulnerable groups. Second, a quite 'passive' orientation of traditional active labor market policies with steps towards activation in labor market policies being rather hesitant and inconsistent both in legislation and implementation (with regard to both "carrots" and to "sticks"). Both active and passive labor market policies in Germany still encourage inactivity and long-term benefit receipt.

In terms of governance, the state has assumed a stronger role in activation with some services contracted out to private providers. This meant smaller influence of the social partners on active and passive labor market policies. At the same time, a general trend towards more flexibility in sectoral collective bargaining leaves more regulatory weight to the role of firm level agreements. The basic structure of employment protection, unemployment insurance and unemployment assistance as well as activating labor market policies is defined by legislation so that there is no "market for insurance" with competing providers.

Despite the fact that the German system of employment protection has undergone marginal change, and both active and passive labor market policies have been reformed considerably in recent years, it seems plausible to expect future change. On the one hand, the current institutional arrangement of the labor market is not (yet) conducive to employment creation and overcoming persistent inactivity and labor market segmentation. In fact, the current system results in a growing segment of flexible or partially subsidized employment that tends to crowd out regular em-

ployment and may undermine the stability of both the institutional arrangement in terms of employment protection and the fiscal stability of social security. In this sense, the current arrangement may prove to be less stable than is often assumed. Hence, given the fact that non-employment and benefit dependency are associated with high non-wage labor costs and taxes, the need for future reforms remains high. Therefore, we would expect further changes continuing the path of gradual reforms in employment protection, stronger activation of benefit recipients and a growing role of tax financed basic income protection as opposed to the contributory social insurance of earnings-related unemployment benefits. Regarding the governance of labor market policies, the current system that differentiates between active schemes for the short- and long-term unemployed, and the joint local administration of the Federal Employment Office and the municipalities to activate the long-term unemployed does not seem to be a stable arrangement with good governability.

Table 12: Chronology: Major Reforms in Unemployment Insurance, Unemployment Assistance and Active Labor Market Policy (1990-2006)

Year	Reform	Details/Background
1991	Contribution Rate Adjustment Act	Increase of Contribution Rate to UI from 4.3% to 6.8% from April 1991; Decrease of Contribution Rate from 6.8% to 6.3% from January 1992.
1991	Amendment to the Employment Promotion Act	From July, the age limit for receiving Transitory Benefit (Altersübergangsgeld) is reduced from the 57 to the 55 years. Duration of eligibility is increased correspondingly from 3 to 5 years.
1993	Amendment to the Employment Promotion Act	Intensification of quality assessment of ALMP training schemes; besides an assessment of individuals' access to training, a general evaluation for appropriateness of the measure for labor market policy is introduced; regarding further training, the possibility for a second promotion are limited through additional temporal requirements (waiting periods); A paragraph regarding employers' compulsory refund of Unemployment Benefits (UB) to older benefit recipients is re-established; sanctions (benefits suspended) due to (intended/grossly negligent causation of unemployment) reduce the period of UB eligibility at least about 25%; severance payments reduce the period of UB eligibility even more; apart from failure to report, the claim for benefits are suspended if a jobcentre's request to participate in a measure for work counseling is ignored; specific ALMP schemes for former GDR region
1993	Budget Law 1993	For 1993 the contribution rate into FEA is increased from 6.3% to 6.5%
1993	Federal Act on Budget Consolidation Program or "Solidary Pact"	"Short-Term Work Benefits" (SWB) is only granted for more than 6 months if the recipient of SWB is available for work and the employer agrees to another occupation; more intense assessment of recipients by PES; the previous bi-annual adjustment of earnings-replacement benefits in the East is now annual; provision of subsistence can not only be claimed through work, but also through work opportunities; Special work opportunities should be created especially for assessment of willingness to work;
1994	First Act to Realize the Saving, Consolidation- and Growth Program (1. SKWPG)	PES to co-operate closer with Municipalities' Social Assistance Agencies; BA can grant permission to run profit-oriented job agencies; From 1st April 1994 to 31st March 1996, BA grants temporary permission for placement services in model regions; For executive employees, FEA is must grant permission for placement services for higher positions; previous claim for Maintenance Allowance (MA) during participation in training schemes is now at PES discretion; Rate of MA is reduced from 73%/65% to 67%/60% of net earnings; Reduction of SWB from 68%/63% to 67%/60%; ALMP subsidies for employers' costs for pension contributions to short-time workers are abolished; Bad Weather Benefit (BWB) reduced from 68%/63% to 67%/60%; period for which BWB can be granted is cut down; participants of direct job creation schemes (JCS) can even be placed into temporary jobs, rejection without important reasons leads to benefit suspension when becoming unemployed; Reduction of UB (Arbeitslosengeld) from 68%/63% to 67%/60% of net earnings; duration of sanctions that occur before end of 1995 are extended; Obligation to report is strengthened; Reduction of "Unemployment Assistance" (UA) from 58%/56% to 57%/53%; "genuine" UA is limited to 1 year
1994	Employment Promotion Act 1994 (BeschfG 1994)	General permission to run private, profit-oriented job agencies; BA wage subsidy to JCSs is determined by 90% of agreed standard wage rate; wage subsidies (JCS) for older employees; Until end of 2000 unemployed persons can take part in short-term training programs without losing UB/UA claim; Rule according to which unemployed persons above 58 do not have to be available for job placement under certain circumstances is extended by 5 years; employed persons reducing their work time to below 80% of agreed standard work time (part-time) and become unemployed within 3 years after part time entry are treated (UB/UA) as if they became unemployed from previous full time occupa-

		tion; extension of sanctions remains in force until end of 2000; recipients of UA performing voluntary community work, do not lose eligibility for UA; "Productive Employment Promotion" (PEP) is extended by the fields "Breitensport" and "Free Cultural Work"; Until end of 1997, activities of hard-to-place unemployed in the areas Environment, Social Services and Youth Aid is incorporated into PEP;
1994	Act on the Adjustment of the Employment Promotion Act in the Area of Construction	Contrary to the rule of 1st SKWPG, BWB is regrantd for the months March and November. BWB will ultimately be abolished with the end of the year 1995 (previously: end of February 1996)
1994	Second Law to Realize the Saving, Consolidation and Growth Program	"Wage Gap Principle" is restricted to households with up to 5 persons (previously 4 or more);
1996	Second Law for the Adjustment of the Employment Promotion Law in the Area of Construction	Instead of abolished BWB, BA pays "Winter Loss Benefits" amounting to usual BWB (67%/60%); Winter Benefits amounting to 2 DM per hour are also granted to top-up Winter Loss Benefits
1996 (April)	Unemployment Assistance Reform Act	Only the long-term unemployed can be placed into JCSs; Claim for Anschluss-UA remains valid for 3 years (previously 1 year) if during this time an UA payment has not been executed due to lack of need; Claim for UA is suspended if older unemployed being eligible for old-age pension without reduction do not submit a pension application within a month; Training measures for recipients of UA are introduced, e.g. for assessment of willingness to work; recipients of UA can be placed into seasonal occupations in low-wage jobs; individual market value rating of the long-term unemployed is replaced by minus-adaptation of 3%
1996 (Aug.)	Act on Old-Age Part-Time Work/Gradual Retirement Revised	Employers' compensation for lower earnings and pension reductions due to employees over 55 working part-time are refunded by BA if an unemployed person or trainee (after completion of vocational training) is hired to replace part-time worker
1996 (Aug.)	Act to Reform Social Assistance	Social Assistance Agencies can facilitate employment of assistance recipients by allowances to the corresponding employer or other suitable measures; if a recipient takes up a job on the general labor market, the agencies can grant him or her monthly allowances for a maximum of 6 months; wage gap Principle is intensified further;
1997	Growth And Employment Promotion Act	No adjustment of reference values of benefits in 1997
1997	Annual Tax Act	Within the scope of means-testing (UA), BA is allowed to request information on unemployed person's assets from financial institutions
1997 (April)	Act on the Reform of Employment Promotion	New training measures for improvement of job market integration prospects and assessment of willingness to work are introduced; Integration Contracts are introduced as a new instrument for employment promotion; PES can grant wage subsidies for start-up employers to facilitate employment of previously unemployed persons for unlimited period; Structural SWB is extended to end of 2002; Promotion of JCSs in commercial sector is only granted, if the measure is given to a business company; subsidization of JCS is reduced to 80% of comparable non-promoted occupations; criteria regarding "suitable" jobs are tightened and are directly regulated in the law; period of claim for UB is reduced; Redundancy Payments, compensations or similar benefits are credited against half of UB;
1998	Act on the Reform of Employment Promo-	Employment Promotion is codified and integrated into the 3 rd Book of the Social Code as SGB III; Benefits to employees, employers and to institutions respon-

	tion	sible for employment promotion measures are partially changed or complemented; UB claim can only be gained through contribution periods. Assessment periods for determination of UB amount is extended to 12 months (previously 6) and includes all those periods in which obligation to insure existed; claim-depreciating effect of sanctions is intensified; "Partial UB" are introduced; For integration of needy employees, the employer can apply for "Settling-In Allowance" as a subsidy for wage; the corridor for wage subsidies to JCS providers is increase from 50 - 75% to 30 - 75% of relevant wage;
1998	First SGB III (Social Code Book 3) Adjustment Act	Also benefit recipients who have only been unemployed for 6 months, can be placed in JCS; Temporary special JCS regulations for a 100% allowance (East) combined with reduced working hours is extended until end of 2000;
1998	Act on the Protection of Flexible Working Time	Some aspects of old-age part-time are changed, such as: Eligible are those persons who move to old-age part-time before 31st July 2004; In case of blocked old-age part-time work, the "Tarifvorbehalt" is restricted to periods of more than 3 years (previously 1 year)
1998 (Aug.)	1st Act to Adjust the Medical Product Act	If a recipient takes up employment covered by Social Security or Self-Employment, social assistance agencies can grant the recipient monthly allowances for a maximum of 12 months (previously 6 months); An experimental clause, which is valid until 31st December 2002, allows to deviate from this regulation;
1999	Act on Social Insurance Correction and Protection of Employee Rights	Expenditures for government program for reduction of youth unemployment are not covered by government, but by BA
1999 (April)	Dismissal Compensation Reform Act	Intensified accreditation of dismissal compensations for UA is abolished
1999 (April)	Act to Reform Minor Jobs	The wage limit for minor permanent occupation is fixed at 630 DM per month
1999 (Aug.)	2nd SGB III Adjustment Act	Benefit to support start of self-employment is uniformly granted for 6 months; Reasonable daily commutes are re-established at former level of 2,5 or 2 hours respectively; The obligation of unemployed persons to refresh their personal unemployment registration every 3 months is abolished; The regulation for 3-year protection of level of UB/UA in case of low-wage employment is introduced; For placement of unemployed persons in JCSs an unemployment of at least 6 months within the last 12 months is sufficient;
2000	3rd SGB III Adjustment Act	Genuine UA is abolished. Only unemployed persons who were eligible for UB are eligible for UA thereafter (Anschluss UA)
2000	Act on Further Development of Old-Age Part-Time	part-time employees get access to old-age part-time; Replacement requirement for BA-subsidized old-age part-time is eased;
2000 (July)	2nd Act on Further Development of Old-Age Part-Time	Law for Old-age part-time is changed regarding (amongst others) period of validity (extended) and maximum period of claim (prolonged); Regulation according to which unemployed persons above 58 have possibility to receive UB without being "available" is extended by 5 years;
2000 (Dec.)	Act on the Improvement of Co-operation Between BA and Social Assistance Agencies	The improvement of co-operation becomes an explicit task of the local responsible employment agencies and the responsible bodies of social assistance; new clause on experiments facilitates regional pilot projects
2002	JobAqtiv Act	Compulsory unemployment insurance also comprises: Periods of receipt of pension due to full reduction in earning capacity as well as periods of receipt of Maternity Benefits and of care and education of a child below 3 if through one of these cases an insured employment was interrupted; Recipients of UB/UA can take up voluntary community work without losing UB/UA claim; Unem-

		ployed persons who, upon job offer by BA, do not arrange an interview immediately, miss an interview or prevent interview success through their behavior are sanctioned; "Market value rating" (Marktwerttaxierung) is modified; Upon registration as "unemployed" a profiling of the unemployed is carried out and resulting further steps are fixed in integration agreement/contract; EOs have to ensure third-party for difficult to place unemployed persons; Application of all instruments of labor market policy is possible without waiting periods; JCS placement is possible without waiting time; a lump-sum wage subsidy is introduced;
2002	Unemployment Assistance Regulation	Maximum level of assets not taken into account in means-testing when unemployment assistance is fixed
2002 (April)	Act to Facilitate Election of "Employee Representative" into Supervisory Board	Conditions for permission for private training places and job centers are abolished; private job agencies may charge placement fee (in case of success) of up to 2.500 €. Unemployed on UB/UA are granted placement vouchers after 3 months of unemployment;
2003	First and Second Act on Modern Labor Market Services (Hartz I and II)	Employees must register "unemployed" with BA immediately; EOs have to establish at least one "Personnel Service Agency" (PSA); For new contracts new rules apply including equal treatment of agency workers and regular workers; "Education Vouchers" are introduced; Anschluss UA is abolished; benefit for UA recipients during training is cut down to last received UA payment; For unemployed without familiar commitments a move to another place is "reasonable" for employment search; Burden of proof for job exit or rejection is redistributed; sanctions due to job exit still 12 weeks, sanctions due to job rejection are scaled; UB and other benefits are no longer adjusted to wage level; Assessment of neediness of UA is tightened; Unemployed above 50 terminating unemployment by taking up a standard waged occupation can claim wage security benefits; Employers occupying older unemployed for the first time are freed from contribution to UI; Age limit from which temporary work contracts without time limit can be concluded with older employees is reduced from 58 to 52; "Business Start-Up Allowance" (Me Inc.) is introduced; Regulations for "Minor Occupations" are eased (400 € per month).
2003	Basic Maintenance Act (GSiG)	For assurance of subsistence in the age of 65 and above and in case of permanent reduction in earning capacity persons regularly living in Germany can receive means-tested benefits according to new Basic Maintenance Law (Grundsicherung)
2004	Act on Labor Market Reforms	Maximum period of UB claim is shortened to 12 months and to 18 months for persons above 55 (effective in 2006); Until this new regulation comes into force, the refund duty of employers to FEA regarding dismissals of long-time employed older employees is tightened;
2004	3rd Act on for Modern Labor Market Services (Hartz III)	UB and benefit during ALMP training are combined to a single benefit from 2005; For UB claim a standard previous insurance period of 12 months (to be fulfilled within 2 instead of 3 years) applies; From February 2006, Military or Civil Servants are insured in unemployment insurance; JCS and "Structural Adjustment Measures (SAM) are combined to a single instrument. Promotion in SAMs are abolished. In JCS employed persons do not underlie obligation to insure with BA and can therefore no longer claim UB; Criteria for self-exerted effort of unemployed person is sharpened; Besides usual sanctions, additional reasons are established from 2005 (e.g. insufficient effort); Old-Age Part-Time Law is partly changed from July 2004; organizational changes within BA
2005	4th SGB III (and other laws) Adjustment Act	Testing period for "Placement Voucher" is extended until end of 2006 (previously 2004)
2005	4th Modern Labor Markets Services Law	Old UA is abolished and combined together with MA for employable persons to a single benefit called "Arbeitslosengeld II" (new UA) amounting to Social Assistance level; Eligible for new UA are employable needy persons and persons

		living together with them forming a needy community; Only persons between 16 and 65 years are eligible for new UA; Regular rate amounts to 345 € (west) and 331 € (east) for singles, for adult partners 90% each, for children below 14 years 60%, for children aged 14 and for other members of the needy community 80% of the regular rate; Costs for accommodation and heating are partially funded by the municipalities, the rest by federal government provided they are adequate. In case of UA receipt within 24 months after end of UB receipt, a monthly extra allowance on top of UA can be claimed; Employable needy person has to participate actively in all measures for his/her own integration, especially he/she has to conclude an integration contract; Every possible work (even below commonly agreed hourly wage) and every measure conducive to his/her integration into a job is reasonable; "Job Entry Benefits" as financial incentive to take up employment is introduced; Regular rate of UA is cut down by 30% for those who, in spite of instructions about legal consequences, refuse to conclude an integration contract or ignore the duties in the same without important reasons; UA rate is cut down by 10% for those who ignore certain requests;
2006	5th Act to Adjust SGB III and Other Laws	The possibility for receipt of unemployment insurance benefit and unemployment assistance under easier conditions for needy persons from 58 years and above is extended until end of 2007; For early unemployment registration a standard registration term of at least 3 months prior to job termination applies independently of individual "Terms of Notice"; BA obligation to establish at least one PSA is abolished; Following measures/instruments are extended: 1) Business Start-Up Allowance, Me Inc. (June 2006); 2) Promotion possibilities regarding Further Training of older persons (end 2006); 3) Commissioning of responsible bodies for integration measures (until end 2007); 4) "Earnings Protection" for older employees (until end 2007); 5) Exemption of employers from FEA contribution when employing person above 55 for the first time (until end 2007); 6) UB for unemployed persons above 58 under easier conditions;
2006	1st Act to Amend SGB II and other laws	Persons coming to Germany to receive ALG II are excluded from benefits; young adults are redefined as part of their parents' needy household; setting up a single household by young adults is to be approved by the administration; ALG II is increased to 345 € in Eastern Germany as of 1st July 2006.
2006	Budget Act	Employers' contributions for mini-jobs raised from 25% to 30%; reduction of contribution rate to unemployment insurance reduced from 6.5% to 4.5% as of January 2007; new arrangement on Federal government's BA deficit coverage
2006	Act to Develop SGB II	Reassignment of burden of proof regarding adults living together; no benefits for persons not available due to absence from place of residence without permission; more generous exemption of old-age savings from means-test; immediate job or training offer when benefits are claimed; stricter sanctioning provisions affecting total benefit, not only regular costs of living allowance (Regelleistung), stronger sanctions in case of repeated misconduct within one year: cut by 60% or total suspension of benefits, particularly strict provisions apply to young recipients; replacement of Me Inc. and bridging allowance by new enterprise start-up grant (nine months of ALG I plus 300 €, possible extension by six months with 300 €)

Source: authors' compilation.

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