Social Protection in Germany: Current challenges and lessons learnt from an ongoing reform process
By Roland Hackenberg

Background

About a decade ago, most European welfare states were considered to be in deep crisis, resistant to restructuring and retrenchment. With a growing number of unemployed, an ageing society and an oversized bureaucracy, public spending was on the increase while at the same time, the tax base and the number of contributors to the social security system were steadily decreasing. In addition, Germany was confronted with the burden of reunification, leading to an expansion rather than a reduction of traditional instruments of labour market policy. Two years after reunification, the former East German labour force of close to 10 million people had shrunk to about 6 million. This resulted in the perceived need for large financial transfers from West to East in order to meet a growing social crisis and prevent massive migration to the West.

However, since then, a series of reforms have taken place. Especially regarding labour market policies, most European welfare states have been changing towards a reduction of transfer payments and an increased importance of activating instruments (Dingeldey 2009:8). In Germany, this policy shift happened mainly after the 1998 elections. With 4.2 million people out of work in 1998, unemployment was one of the most prominent topics in the election campaign. During their two terms in office, the new Social Democrat-Green government coalition produced two waves of social policy reforms. Firstly, the “Job AQTV Act” of 2002, strengthening job-search activities, job profiling and reintegration contracts for unemployed benefit claimants as well as the access to wage subsidies, training programs and business start-up options, so called “Ich-AG” (=“Me-PLC”). Secondly, the Hartz commission (named after the chairman of the commission, Peter Hartz, a personnel manager at VW) elaborated the “First to Fourth Law for Modern Services in the Labour Market”.

This new legislation came into force between 2003 and 2005. It has been described as the largest paradigm shift in German social policy after World War II. It moved away from the concept that unemployment aid is mere charity. Instead, a new approach was installed with unemployed as “clients” who, on the one hand, have a legal claim to receive state support and, on the other hand, have to fulfil certain responsibilities/conditions. At the heart of this new approach is the concept of “promoting and demanding”, comparable to the British welfare concept of “rights and responsibilities” under the Blair administration (Clasen 2005: 73). “Promoting and demanding” established an activating rather than maintaining social welfare policy for long-term unemployed. It turned away from the previous concept of status protection and individually calculated benefits according to former earnings, towards a means-tested basic income support based on lump-sum payments. This income support is paid as a conditional cash transfer mainly to those unemployed able to work and with (limited) self-help capacity.

This paper aims to provide an overview of Germany’s current social protection system with a strong focus on unemployment benefits, especially regarding the conditional cash transfer instrument. It discusses the main arguments and lessons learnt within this ongoing reform process. Against this background, the controversy regarding graduation mechanisms and the “right” set of conditions and incentives to re-integrate beneficiaries into the job market is especially highlighted. Summing up, this paper draws lessons learnt from the last decade of social policy reform in Germany. By doing so, it aspires to provide relevant insights about the trade-offs between costs and benefits of the current system that hopefully could enrich the ongoing discussions and reform processes within developing and emerging economies.
Instruments of social protection in Germany

The current social protection system in Germany basically consists of two pillars:

1. a social insurance system tied to formal employment with benefits or services in recognition of peoples’ contributions and
2. a tax-funded unemployment and social assistance system to guarantee a minimum subsistence level.

The public insurance schemes

There are five different insurance schemes within the public social insurance system: public health insurance, nursing care insurance, accident insurance, pension insurance and unemployment insurance. Contribution to these schemes is mandatory, with contributions of employees related to their monthly earnings. Contributions of the unemployed or unable to work are fully paid by the state while self-employed usually only have to contribute to a public or private health and nursing insurance scheme. There are several underlying principles within the German Social Insurance System: the principle of “compulsory coverage” establishing mandatory contributions, leads to 90 per cent of the population being insured while the principle of “funding by contributions”, with contributions equally shared by employers and employees, aims to achieve a balanced financing of the system (since July 2009, the monthly social insurance rates from salaries are 14,9 per cent for health insurance, 2,8 per cent for nursing care insurance, 19,9 per cent for pension insurance and 2,8 per cent for unemployment insurance). Another principle is the “self-governing principle” of the different public-law corporations managing the public social insurance schemes under their own responsibility and with legal control by the federal government. Finally, the “principle of equivalence” applies to the pension insurance scheme, linking the size of contributions to the amount of benefit payments received at the end of working life.

Unemployment benefit I and II

Social protection for the unemployed comprises an insurance-funded (Unemployment Benefit I or UB I) and a tax-funded system (Unemployment Benefit II or UB II). Both systems are tailored for people with (limited) self-help capacity, able to work and to enrol in active labour market measures which aim to support their graduation from these schemes.

Unemployment benefit for formerly insured employees (UB I) is managed and implemented by the Federal Employment Agency (Bundesagentur für Arbeit, BA). The BA is also in charge of the active labour-market programs in Germany. If deficits occur, federal government has to balance out the annual BA budget (Clasen 2005: 55). UB I, as an insurance benefit of about 60 per cent of the last net wage, is paid monthly during the first year of unemployment. The most important condition for receiving full-length UB I is that the jobless person has contributed to the unemployment insurance fund for at least two years within the last three years. Shorter contribution periods lead to a reduction of months of UB I benefit payments. There are exceptions for older unemployed regarding the length of UB I, with benefit payments of 15 months for over 50-year-old, 18 months for over 55-year-old and 24 months for over 58-year-old.

Unemployment benefit II, also known as “Hartz IV” (named after the forth law elaborated by the Hartz commission) was introduced in 2005. The new means-tested benefit Hartz IV abolished the former system of unemployment benefits, merging former “unemployment aid” with social assistance for those able to work. Basically everybody not receiving UB I and able to work – e.g. the unemployed but able to work or the working but with incomes under a certain threshold – is entitled to receive UB II. The monthly paid benefit for single headed households consists of a flat-rate payment of currently 359€. This standard rate (Regelsatz) is calculated in July every year and linked to the development of public pension payments. In addition, “appropriate” housing and heating costs are paid as a top up to the standard rate as well as certain supplement payments such as for former UB I claimants during their first two years of UB II, single parents or pregnant women. Couples sharing a household and children from 15 to 18 years old receive a slightly reduced standard rate while household members not able to work (primarily children under 15 years old) receive a reduced standard rate called “social benefit” (Sozialgeld).

Accompanying the actual benefit payments, claimants are entitled to a number of “activating” measures. These measures aim to create incentives and even assert pressure on unemployed persons to quickly re-integrate into the job market. But they are also defined as “rights” of claimants to e.g. receive counselling or training. An emphasis is placed on case management and active participation of job-seekers which have to sign a so-called “integration agreement”. This agreement documents the commitments of claimants to engage in job-seeking activities as well as the supportive measures they are entitled to receive. UB II claimants, in principle, have to accept any legal job offered and there are benefit sanctions and/or periods of exclusion from UB II for those refusing a job or training offer.
In order to activate long-term unemployed that are likely not able to integrate into the job market in the near future, works in the general public interest of 3 to 8 hours per day are offered to claimants. These jobs, in their majority within the public or third sector, usually do not give rise to proper employment relationships but a top-up to UB II is granted of 1 to 2,5€ per hour (which has led to the colloquial term of “One-Euro-Jobs” for this measure). Young unemployed are specially targeted with more intense counselling, training measures and/or child care support (in the case of young single parents). But young unemployed also suffer quicker and stronger sanctions if they do not cooperate. All UB II recipients are allowed to earn an extra 100 Euros per month additive to the public benefits received. Higher earnings reduce the monthly rate of UB II benefits.

While the BA is implementing UB I, 346 “Job Centres” where created in 2005 to administer and implement UB II. These Job Centres, also called “Arbeitsgemeinschaften” or “ARGEn”, are joint agencies combining former government supported work agencies and municipal social assistance offices. While the government pays for the monthly UB II benefit as well as for complementary re-integration measures (such as the “One-Euro-Jobs”), local administration basically shoulders the costs for housing and heating and offers counselling services i.e. addiction or debt counselling. In addition, there are 69 so-called “Optionskommunen”. These are municipalities that have chosen to keep the administration of UB II fully in their hands. After a Constitutional Court decision in 2007 declaring the ARGEen unconstitutional (mainly due to a lack of transparency of competences), the government is currently working on a reform of the implementing structure of UB II.

Social Assistance

All persons unable to work (e.g. chronically-ill, disabled persons, the elderly, children living with relatives) and not receiving other public benefits, are entitled to receive social assistance. These people do not have sufficient self-help capacity and are dependent of long-term state support to live above the subsistence level. Social assistance is an unconditional transfer (in-kind, cash or vouchers). People from 15 to 64 years old which are able to work or live in a household with somebody able to work (and thus entitled to social benefit payments within UB II) are excluded from social assistance. In 2008, about 860,000 Germans received social assistance with around 4.3 billion Euros spend on this instrument (Statistisches Bundesamt 2010). Social assistance is funded by municipalities which maintain their own municipal social assistance offices. As this paper focuses on social protection mechanisms for people with self-help capacity in order to discuss lessons learnt regarding incentives, conditions and governance processes, social assistance schemes are not discussed further.

Challenges and lessons learnt from the system

In 2008, total public expenditure for all tax-funded social benefits was 40.5 billion Euros. Around 7.6 million people received these benefits out of which 6.6 million lived on Hartz IV payments (Statistisches Bundesamt 2010). Since its introduction in 2005, the new unemployment legislation has been under strong criticism and its further development is discussed by different social and political groups.

For some, the Hartz reforms and especially the introduction of UB II under Hartz IV have been a mayor success. According to them, the reforms have:

- Improved the efficiency of supporting claimants by merging former unemployment aid and social assistance to one program (UB II) implemented at one-stop shops (Job Centres/ARGEen).
- Increased the incentives to take up employment and reduced long-term (= longer than 12 months) unemployment a 41.3 per cent since 2005.5
- Supported positive trends during the last economic boom with the creation of 1.3 million new employments compared to 700,000 during the previous boom phase.
- Improved counselling and support to the unemployed.
- Given municipalities increased authority to engage in employment activities.

For others, the Hartz reforms have failed to meet their objectives. These groups mainly point out that:

- Several studies show that UB II has caused a reduction of benefits for up to 59 per cent of former unemployment assistant beneficiaries.6
- The reform has broken with former principles of social justice. It has fostered the fear of losing social status within broad parts of society and increased (child) poverty in Germany.
- The obligation to accept any job offered and instruments such as “One-Euro-Jobs” have increased the pressure on average wages and the creation of marginalized employment.
- Within the concept of “promoting and demanding”, the support and counselling of claimants within the ARGEEn shows strong deficits while at the same time, the “demanding” element with sanctions and the pressure to accept jobs is overemphasized.
- Despite official statistics and placement efforts by Job Centres, leaving long-term unemployment is still a major challenge for those unemployed longer than a year.7

---

5 Süddeutsche Zeitung (08.01.2010); IAB 2009
6 IAB 2007b: 22f; DIW 2007
7 IAB 2009
Apart from these general lines of arguments, a number of concrete issues and proposals to “reform the reform” are currently discussed. In the following, three issues of this public debate will be discussed in order to show experiences and lessons learnt regarding the German social protection system.

1. Conditions: Balancing the right to social protection with the need to provide adequate incentives for work

Compulsory work schemes such as One-Euro-Jobs and the obligation to basically accept any job offered are facing strong criticism. Many assert that within the concept of “promoting and demanding”, policies towards improving individual support to the unemployed and creating new jobs that ensure a minimum standard of living are still underdeveloped while a strong emphasis is placed on “demanding”. In short, crucial questions are:

- Is social protection a human right for all those in emergency situations or do state transfers imply certain responsibilities for the unemployed which can be sanctioned in the case of non-compliance?
- Should more pressure be asserted on UB II beneficiaries to accept any available job or is their unemployment owed to other reasons, e.g. periodically occurring economic crisis or a lack of child care opportunities which make it impossible for certain parts of society to find a new job such as the unemployed above 50 year old and single parents?
- Which conditions should and can be imposed on UB II claimants and which are the right instruments to ensure a quick graduation from UB II?

There are many answers to these questions, depending of the stakeholder asked. Nevertheless, interesting lessons learnt from this debate could be:

- On the positive side, “promoting and demanding” seems to deliver first results: In recent years, there has been a positive trend in the job market, with a strong reduction of unemployment which is not only owed to the economic boom until 2008. In addition, job placement seems to have improved with the same number of vacancies in 2009 compared to 2005 but with 1.3 million less unemployed.8
- The paradigm shift towards an activating social policy is in principle heading into the right direction. The new customer orientation and counselling of the Job Centres stand for positive changes, moving away from the mere administration of databases and benefits for unemployed persons to finding individual solutions for activating the self-help capacity of beneficiaries to support their livelihoods.9
- The notion that UB II receivers are generally too lazy to work and should be forced to accept available jobs is decreasing as it fails to encompass the multidimensional reality of the problem. Integration agreements and existing sanction mechanisms do create incentives to engage in job-seeking activities. Many stakeholders argue that no further sanction mechanisms are needed but the better implementation of the already existing ones.10
- The element of “promoting” still falls short although it is one of the most important issues in order to make “Hartz IV” a success. Counselling and promotion which address the individual situation and needs of claimants are not sufficiently implemented yet. This especially holds true for unemployed under 25, single mothers and older unemployed. Fewer claimants per case manager in general as well as better child care opportunities, improved debt and addiction counselling or better job application training would be important issues yet to be strengthened.
- The success of activating measures to re-integrate long-term unemployed in the regular job market such as One-Euro-Jobs or integration allowances for employees (= a subsidy paid to employers for hiring UB II claimants) have been controversially discussed. Despite legitimate criticism, integration allowances have created insured employment in 70 per cent of the cases11 and One-Euro-Jobs have brought long-term unemployed closer to the job market as well as improved their self-esteem.12
- Nevertheless, evidence suggests that One-Euro-Jobs do cause a crowding out of regular jobs, especially in the care and service sectors.13 A growing number of unemployed accepting jobs for less payment and a growing number of “working poor” (= people working full time and at the same time receiving Hartz IV benefits to top up their income to subsistence level) are most likely increasing the pressure on average wages. This leads to the discussion to introduce minimum wages in Germany.
- The current social protection system of Hartz IV is causing enormous costs. In 2008, public spending for social assistance and UB II benefits reached 40.5 billion Euros. Nearly 60,000 people worked in the 346 Job Centers around the country, attending about 6.6 million UB II claimants.14 This highly bureaucratic and complex German system is hardly transferable to other countries and within Germany the debate on cost-effectiveness is conducted very controversially.

---

8 IAB-Kurzbericht 2009
9 Die Zeit (28.01.2010)
10 Die Zeit (28.01.2010)
11 IAB 2008
12 Landeszentrale für politische Bildung
13 IAB 2007a: 43; Landeszentrale für politische Bildung
14 Statistisches Bundesamt 2010; Frankfurter Allgemeine Zeitung (18.02.2009)
could be rewarding is the assessment of costs and benefits of specific conditions and graduation mechanisms of Hartz IV such as One-Euro-Jobs or integration agreements. By doing so, cost-effective instruments could enrich or even foster reform discussions on social protection schemes within developing countries. However, many times sufficient scientific data is still lacking to draw clear conclusions on the cost-effectiveness of German social protection instruments.

- Although activating measures have proven to increase job-seeking activities of the unemployed, they can only be successful if they meet a demand in the labour market. In times of strong economic crisis, these measures should therefore focus more on increasing qualification than asserting pressure to look for a job.

2. Calculating benefits for UB II claimants

Calculating the amount of transfer payments is a crucial question for social protection systems. It is a trade-off between providing the right incentives for unemployed to take up employment, preventing people from living under the subsistence level and being financially feasible. Regarding Hartz IV, the “standard rate” is the core parameter for the scheme’s transfer payment as it defines the level of monthly payments for UB II claimants as well as for other persons living in the household (e.g. partner and/or children). The standard rate is calculated yearly according to the needs of an average single-headed household earning an income in the last quintile of wage groups. Calculating benefit payments according to the income level of an average household and giving these flat-rate payments to all UB II beneficiaries alike (instead of calculating transfers according to individual needs) has been one of the mayor changes introduced by the Hartz reforms. Defining the “minimum living standard” necessary to lead a decent live is nevertheless a very controversial issue.

Possble lessons learnt regarding the calculation of benefits for UB II claimants could be:

- Advocates of the current system claim that flat-rate payments have reduced administrative procedures and have empowered UB II claimants to take their own consumer decisions. In contrast, during the pre-Hartz system every single additional purchase such as e.g. furniture or clothing had to be approved. Currently, the new government of Christian Democrats and Liberals is assessing the possibility to introduce flat-rate payments for housing and heating costs, taking into account regional price differences.

- Critics of the system argue that the standard rate is too low to prevent a quick decline of social status in case of unemployment. According to them, the low standard rate has increased poverty levels in Germany. Especially child poverty and social benefits for children are strongly discussed. Until now, social benefits for children are merely calculated as a (lower) percentage of the standard rate, not taking into account their special needs and extra expenses such as additional clothing or school books. Therefore, the Constitutional Court is expected to deliver a judgment in February 2010 on the level of benefit payments for under 14-year-olds which most probably will conclude in an increase of payment rates.

- Calculating benefit payments always is linked to the consideration of regular incomes earned within the lowest quintile of the labour market. In Germany, a law defines the compulsory gap between low income earners and receivers of transfer benefits. The benchmark is a family with three children and one member of the household earning an income within the lowest wage group. In order to avoid negative incentives to take up employment, public transfer payments for this family should never be higher than the income that would be earned through regular employment according to the benchmark calculation.

3. Implementing UB II: Allocation of rights and duties of government and municipalities

The Hartz Reforms also established a new cooperation between state and municipal authorities in the form of Job Centres/ARGEn. These local working groups offer UB II claimants a one-stop-shop assistance, with one single agency attending their needs. Despite the very positive experiences of this cooperation, unclear and vague legislation has led to a Constitutional Court judgement which declared ARGEn unconstitutional in 2007 and requested government to elaborate a new regime for their cooperation with municipalities until 2011. Currently this reform is under discussion, with the government aiming to keep the existing structure under a new name (Centres for Work and Basic Protection, ZAG) and a new, more precise legislation (Bundesministerium für Arbeit und Soziales 2009). In addition, the government has showed clear signals to maintain the different local schemes by cancelling the original time restriction until 2013 for the 69 “Optionskommunen”.

---

15 IAB 2009
16 Bundesregierung 2009: 82f
Lessons Learnt from this debate could be:

- Before the reforms, social assistance programs for unemployed (not receiving enough assistance through other public programs) where fully funded by municipalities. This created a vicious circle in already poor regions: High unemployment rates and a large number of long-term unemployed increased social assistance spending of municipalities, leading to a lack of resources for regional public investment and, in turn, fostering further employment losses and unemployment. In this regard, the merging of social assistance for unemployed and unemployment aid was a success as it partly reduced the financial pressure on municipalities.

- In general, ARGEs have been a positive experience for municipalities and government, joining up forces and integrating local competencies in the fight against unemployment. Nevertheless, legislation has been vague and the upcoming reform will likely raise new questions. Especially sensitive is the question of power relationships between government and municipalities (e.g. Which stakeholder has the right to determine the specific entitlements of each UB II claimant?). In addition, an increased bureaucracy is expected as claimants have to be able to clearly identify which UB II benefit is coming from which stakeholder (either municipalities or government).

Regarding the different models such as “Optionskommunen” or “ARGEs”, some claim that the Optionskommunen model has empowered local authorities and provides efficient services while others point out that the fragmentation of different schemes for UB II claimants at the local level is complicated and unjust as it does not provide the same services to everybody. Further studies have to find more evidence on this issue.

Outlook

The current debate on reforming Hartz IV is very political and sometimes characterized by strong polemics. Within large parts of the German middle class, the 2005 reform has raised existential fears of quickly sliding down the social ladder into poverty. At the same time, this middle class is the “classic” voter clientele of basically all mayor political parties. Therefore, many reform proposals for Hartz IV nowadays address this clientele with little estimated impact on the majority of UB II beneficiaries. For example, the recent increase of the amount of assets a UB II claimant is allowed to possess without losing his or her entitlement to receive public transfer payments is not a relevant action for large parts of long-term unemployed UB II beneficiaries. In short, reforming Hartz IV can only be successful if decision-makers focus on the specific needs of long-term unemployed and improve instruments and mechanisms tailored to their needs.
Literatur

Bundesministerium für Arbeit und Soziales (2009): Eckpunktepapier: Neuorganisation der Aufgabenwahrnehmung im SGB II. Download


Die Zeit 28.01.2010: Hartz IV: Gesetz der Angst. Website


Frankfurter Allgemeine Zeitung 18.02.2009: Arbeitsgemeinschaften: Neuordnung der Hartz-IV-Verwaltung wird teuer. Website


Landeszentrale für Politische Bildung Baden-Württemberg: Die Ein-Euro-Jobs. Website

Rheinische Post 17.12.2009: BA-Chef Weise „Optionskommunen kein gutes Modell“. Website


Süddeutsche Zeitung 08.01.2010: Hartz IV: Gibt es weniger Langzeitarbeitslose? Website