



Hartz IV in Context: The German Way to Employability

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Theme: Germany's latest labour market reforms, known as Hartz IV, have come into force in 2005.

Summary: In contrast with other European economies such as the Netherlands, Denmark, Sweden and the UK, the reunified Germany was unable to solve its severe labour market crisis during the 1990s. It was only at the end of the 1990s that Germany also started reforms and enhanced employability as a new goal of its labour market policy, thereby following the approach of its neighbours and the forecasted European employment strategy. In 2005 the latest labour market reforms came into force with Hartz IV. In order to describe the new relations between citizens and the welfare state implied by the so-called activating 'labour market policy', Chancellor Gerhard Schröder coined the slogan 'Challenge and Support'. In the following analysis we will try to understand this German way towards employability.

Analysis

The Socio-Economic Situation and the Labour Market

During the 1990s Germany faced a severe slowdown in its economic growth in comparison with other European countries. While Germany's average per capita GDP growth was only 1.2 % in 1991-2001, other European economies (excluding the German Federal Republic) grew by an average 1.9%. One of the reasons adduced for the decline in economic growth is the high financial burden caused by German reunification, which was financed by rising taxes and social security contributions as well as by increasing public debt. Furthermore, commentators have observed that re-unification was paid for at the expense of investments for the future (eg, infrastructure and education).¹

The economic crisis created severe labour market problems. In January 2005 the unemployment rate had risen to 12.1%, with more than 5 million unemployed according to official statistics.² One of the main reasons for this is that, especially in Eastern Germany, the labour market is unable to create sufficient demand for labour. Hence, despite ongoing East-West migration, unemployment in the East is still at 20.5% in 2005. This also partly

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¹ G. Bosch and M. Knuth (2003), 'Das deutsche Beschäftigungssystem im 13. Jahr nach der Vereinigung', *WSI-Mitteilungen*, May, p. 275-283.

² In December 2004 official statistics indicated a figure of 4.46 million unemployed, equivalent to an unemployment rate of 10.8%. The sharp rise in 2005 is mainly attributable to Hartz IV. As a result of this reform former recipients of social assistance who are considered to be capable of working now receive ALG II and are included in the unemployment statistics (<http://www.pub.arbeitsamt.de/hst/services/statistik/detail/a.html>).

explains why unemployment rates in the West have not decreased (at 9.9% in 2005) despite effective employment growth (2.75 million unemployed, or 14.5%, between 1975 and 2002).³

The Political Context

Labour market reform was already overdue when the red-green government came into power in 1998. Without the backing of Keynesian demand management since the 1980s, Germany's active labour market policy was overburdened. It was nevertheless expanded in order to soften the impact of the structural labour market problems caused by reunification. Hence, by the end of the 1990s the Federal Employment Institute's expenditure had risen sharply⁴ and unemployment rates remained at historically high levels.

During its first legislature, however, the red-green government seemed to lack a clear-cut governmental strategy for the labour market, resulting in policy failures and piecemeal reforms.

The establishment of the 'Alliance for Jobs, Vocational Training and Competitiveness', a regular meeting between representatives of the most important industrial unions and employers' organisations and the government, proved to be a failure. Instead of compelling trade unions and employers' associations to attempt to reconcile their conflicting positions by imposing positive or negative sanctions, the federal government conceded major decisions to each of them bilaterally.⁵ Thus a good opportunity for negotiated structural reform had been squandered when the Alliance finally fell apart at the beginning of 2002.

No fewer than 35 changes in Germany's labour market legislation were approved between 1998 and 2002,⁶ mainly isolated reforms that limited insecure employment or adapted German laws to European guidelines in order to enhance employability (the 'JobAQTIV Act', for instance). However, no coherent strategy aimed at implementing large-scale labour market reforms was designed.

At the beginning of 2002 the so-called 'placement scandal' broke out following a Federal Audit Office report in 2002 which revealed that the FES had exaggerated its job placement data. In reaction, the government created a commission on 'Modern Services in the Labour Market' (known as the Hartz Commission after its chairman) in order to overcome the deadlock by externalising the preparation of political decisions.⁷ The Commission's purpose was not to develop an integrated concept for employment creation, but to prepare a project for the reform of labour market administration and services. With certain revisions the Commission's proposals⁸ have been enacted by subsequent legislation, such

³ Bosch and Knuth, *op. cit.*

⁴ In 2003 around 3% of German BIP was spent on labour market policy: €1 billion on unemployment benefits, €1 billion on active labour market policy and €5 billion on labour market administration. See W. Jann and G. Schmid (eds.) (2004), *Eins zu eins? Eine Zwischenbilanz der Hartz-Reformen am Arbeitsmarkt*, Berlin.

⁵ See W. Eichhorst (2002), 'Bündnis für Arbeit-Chancen vergeben?', *Sozialer Fortschritt*, November.

⁶ Jann and Schmid, *op. cit.*

⁷ The chairman and most of the 15 members of the Hartz Commission were representatives of business interests. The representatives of social partners, government and public administration as well as scientific experts only had a few places each. See G. Schmid (2003), 'Gestaltung des Wandels durch wissenschaftliche Beratung. Das "Bündnis für Arbeit" und die "Hartz-Kommission"', in S. Ränge and G. Schmid, *Management of Change in der Politik? Reformstrategien am Beispiel der Arbeitsmarkt- und Beschäftigungspolitik. Ein Werkstattbericht*, Münster/New York/München/Berlin, p. 68-94.

⁸ P. Hartz (2002), 'Der Bericht der Kommission', *Soziale Sicherheit*, September 8, p. 254-260.

as the *Modern Services in the Labour Market Act*, and are referred to as the 'Hartz Reforms'.

The Hartz Reforms⁹

Following the re-election of the red-green government in 2002 the Hartz reforms were implemented and partly re-reformed previous strategies to support employability. However, the reforms either neglect or poorly endow the policies aimed at supporting and developing individual capabilities and, on the contrary, strongly emphasise transfer cuts and workfare aspects. Furthermore, they require the previous restructuring of Germany's labour market administration.

Creation and redirection of labour market instruments

Hartz I and II (implemented in 2003) were aimed at promoting 'new' forms of employment:

- A previous reform carried out by the red-green government, aimed at limiting insecure employment with the so-called 'mini- and midi-jobs', was reversed, with reduced income tax liability being curtailed and social security contributions increased (currently at €400/month, with full liability at only €300/month). However, these measures have been criticised because an increase from around 300,000 to around 4.4 million employees in this type of jobs will merely raise the number of individuals earning low wages and enjoying only marginal social protection. As married women are traditionally the largest group holding insecure jobs, the reform is suspected to be a way of channelling a large proportion of the growing female labour supply towards precarious employment.¹⁰
- The 'Ich-AG' (Me-plc) model is aimed at supporting 'small entrepreneurs' who create their own businesses by providing a monthly allowance which ranges from €600 in the first year to €240 in the third year (to a maximum of €14,400). In 2003 the subsidy was received by around 83,000 unemployed (www.das-parlament.de/2004/09/Thema/004.html). Press reports, however, claim that a large number of these businesses fail, so successful employment creation is actually far lower than suggested by the figures.
- *Personnel Service Agencies* (PSAs) were set up as a new instrument to strengthen the use of temporary employment as a means of job placement. By the end of 2003 there were PSA jobs for around 43,500 unemployed and more than 30,000 temporary staff working for them. Of the approximately 12,400 people who have left the PSAs, 5,400 have started on new jobs, paying statutory social insurance contributions.
- The Hartz reforms have cut back on the high-quality training measures which had been

⁹ The following text, if not otherwise indicated, is mainly based y on Federal Ministry of Employment and Labour (2004), *Annual Economic Report for 2004*, Berlin, and D. Finn and M. Knuth (2004), 'One Stop? Joining Up Employment Assistance and Benefit Administration in Britain and Germany', paper presented at the annual Espanet conference, Oxford, available at

<http://www.apsoc.ox.ac.uk/Espanet/espanetconference/papers/ppr.11A.DF.pdf>

¹⁰ A. Koch and G. Bäcker (2004), 'Mini- und Midi-Jobs - Frauenerwerbstätigkeit und Niedrigeinkommensstrategien in der Arbeitsmarktpolitik', in D. Baatz, C. Rudolph and A. Satilmis, *Hauptsache Arbeit. Feministische Perspektiven auf den Wandel von Arbeit*, Münster, p. 85-103.

in place for several years.¹¹ New instruments, such as the introduction of training vouchers, are aimed at improving both individual choice and self-responsibility. The innovations, however, are counteracted by restrictive changes concerning the eligibility of target groups, the duration of benefit rights and the level of entitlement during an individual's participation in training schemes. Hence, the general reforms can be summarised as being less generous than previously and more restrictive in terms of eligibility.¹²

Reorganisation of the Federal Institute of Employment (BA)

Reform of the German employment service had actually started before the 'placement scandal', but as an immediate reaction to it the board of directors was abolished and the governing body's responsibilities were downgraded to a merely controlling function in 2002.¹³ As part of Hartz I and II job placement services were greatly intensified, but new and more flexible regulations on blocked periods were introduced and applied more consistently. Hartz III, which came into force on 1 January 2004, however, gave the greatest and so far final impulse for the BA to become a modern services provider in the labour market.

In future the BA will operate as the *Federal Employment Agency* and the local FES offices will become *Job centres* which are to serve as 'one-stop shops' for all labour market services. This new model is partly patterned on Britain's Jobcentre Plus concept. It involves the introduction of 'customer management systems' to free specialist staff from routine administrative activity so that they can work more effectively with the unemployed who have 'limited placement opportunities'. Case managers or Personal Advisers identify and tackle employment barriers, and Job Placement Officers work with employers and match the unemployed with vacancies. The new system has been adjusted and modified in the light of operational experience and its impact has still to be evaluated.

Hartz IV and the Creation of Unemployment Benefit II

With Hartz IV what is perhaps Germany's most radical labour market reform came into force on 1 January 2005. Contribution-based unemployment benefits for those who are unemployed for up to 12 months remain unchanged. Those affected are the long-term unemployed and those who are out of work but capable of participating in the labour market. Hartz IV will combine unemployment assistance and social assistance into a single Unemployment Benefit II (UB II), thus ending the coexistence of two different state benefit systems and the sharing of costs between the providers: the municipalities and the Federal Government. So far, the structural reform seems reasonable and necessary. Controversy, however, has emerged concerning the administration of the new benefits and the rash integration of different administrative structures. Protest at the street level is aimed at entitlement cuts and at workfare elements:

- In principle, the job centres are now the only places to which all job-seekers in need of assistance can apply. This, however, has given rise to controversy concerning the role

¹¹ The number of participants in further vocational training decreased already from 722,000 in 1993 to only 251,000 in 2003 (Bundesanstalt für Arbeit: Daten zu den Eingliederungsbilanzen 1998-2003).

¹² See G. Kühnlein and B. Klein (2003), *Bildungsgutscheine - mehr Eigenverantwortung, mehr Markt, mehr Effizienz? - Erfahrungen bei der Neuausrichtung der beruflichen Weiterbildung*.

¹³ See R. Konle-Seidl (2003), 'Von der Anstalt zum ersten Dienstleister am Arbeitsmarkt? Möglichkeiten und Grenzen der Reform der Bundesanstalt für Arbeit', *Gesundheits- und Sozialpolitik*, February 1, p. 22-29.

of the municipalities, which are expected to form 'consortia' with the FEA to provide a single service to the unemployed who depend on services from both agencies. There are now 69 'experimental' districts where municipalities take over full and exclusive responsibility for UB II recipients. In the remaining areas the local 'agencies for work' still have to negotiate with the municipalities to form consortia to which the latter should contribute the 'soft' services not directly related to employment assistance (such as debt and drug-abuse counselling, child-care provision, etc). The municipalities, however, have no obligation to enter such consortia but remain free to deliver their services independently. In any case, since January 2005 the FEA local 'agencies for work' outside the 'experimental' districts are obliged to implement the new benefit. The functioning of these regulations has been questioned as both the problems of clients and the administrative culture of the social administration of municipalities are very different to those of the local FEA offices. Hence, similar reforms in the UK, for instance, had been planned and carefully initiated over several years in order to avoid conflicts and mismanagement.

- The new UB II has been set at the lower benefit rate, which for single adults and single parents is €345 per month in the West and €31 in the East, with additional supplements for children and other adult dependents as well as housing costs. The changes to benefit entitlement have been controversial and it is estimated that up to 1.5 million people face reductions in their entitlements, especially UA recipients who have significant savings or a working partner (*Financial Times*, 2 July 2004).
- The core element in the new benefit system is case management. This involves establishing the specific needs of the individual and on this basis working out an individual offer with the active cooperation of the person seeking assistance. This is steered through an integration agreement, renewable every six months after 2006, or every three months in the case of younger claimants. Failure to enter an agreement results in a benefit reduction of 30% or, for those under 25 years of age, in the complete withdrawal of benefit. Beyond these entitlement cuts, the strictest requirement is that in principle UB II recipients will have to accept any job which they are physically and mentally able to do. Exceptional circumstances specifically laid down in the law apply only if a person has to care for a child under the age of three or a relative. This means, however, that mothers with children over the age of three should in principle enter the labour market.
- In order to improve the employability of mothers, labour market policy now includes the provision of childcare facilities.
- It is estimated that the introduction of UB II will save around €1.5 million/year. The Federal Government wants the funds to be redirected to improve child day-care facilities. In West Germany the insufficient provision of places for children under three years of age is expected to be doubled to 120,000 by 2006 and meet the estimated demand of 230,000 new places by 2010 (<http://www.bmfsfj.de/Politikbereiche/familie,did=19880.html>). So far, however, it does not seem entirely clear whether UB II will indeed save money and provide extra financial resources to the municipalities so that they can employ it to improve child-care facilities.

The Reforms in a European Context

At least in theory the German labour market reforms reflect the main aspects of the EU's employment strategy, one of whose principal goals since 1998 has been to improve employability. But while the 'JobAQTIV Act' constituted a positive interpretation of that goal, namely the support of individual capabilities and improved job quality, one of the main results of the Hartz reforms has been the enforcement of labour-market participation.

The introduction of UB II must be seen as a clear cut-back of benefit entitlements for most of the long-term unemployed, backed by the withdrawal of job protection and increased sanctions. Furthermore, the new forms of employment support the expansion of a low-wage sector. Nevertheless, the reform of the German labour administration can be considered positive in the sense that it improves the quality of placement services, although improvements are still in progress and will have to reconcile conflicting interests before that can operate as a high-quality and inclusive one-stop-service for all the unemployed. At the same time, however, further training as an instrument of active labour market policy is being cut back. Additionally, the promotion of employment for women has been only half hearted: while many policies such as family taxation, child-care provision and school opening hours follow the 'male-breadwinner' model, a significant proportion of the growing female labour force is being channelled into marginal part-time employment. In sum, the Hartz reforms resemble to a greater extent a workfare policy than an enabling approach. Rewording the Chancellors' slogan, Germany's labour-market reforms are more 'challenge' than 'support' to the unemployed.

As these reforms are not embedded in a broader macro-economic strategy aimed at increasing demand in order to create employment, it is more than doubtful that Germany will meet the targets set by the Lisbon Agenda of 2000: an average employment rate of 70% and a female employment rate of 60% by 2010.¹⁴ Hence, in the near future we can expect the development of the German labour market to move away from the high-wage, high-quality and full-employment economies typical of Scandinavia and to start sharing more and more problems with countries such as Spain.

Conclusions: What we have seen so far of Germany's labour market reform will not help groups that have particular difficulties in gaining access to the labour market –low-skill workers and especially women with young children– to become permanently integrated into the employment market. Instead, it will lead them to alternate between long periods of labour market exclusion and precarious and poorly paid forms of employment. Furthermore, unemployment will not be evenly distributed but will concentrate in specific deprived areas. The only difference might be in youth unemployment which in any case is still relatively low in Germany as a result of the apprenticeship system, which combines training, work practice, low wages and a formalised and nationally acknowledged regulation and certification system in many trades and professions. Other than that, however, neither the results of the recent labour market reform nor employment trends in the foreseeable future recommend Germany any more as a model of good practice.

¹⁴ See F. Lefresne (1999), 'Employability at the Heart of the European Employment Strategy', *Transfer*, April, p. 460-481, and M. Ferrera, M. Matsagangis and S. Sacchi (2002), 'Open coordination against poverty: the new EU "social inclusion process"', *Journal of European Social Policy*, March, p. 227-239.