

Hartz' Reforms – Hard reconstructions?

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Introduction

Between 2002 and 2005 the unemployment insurance and assistance scheme of Germany had been altered profoundly. The Volkswagen manager Peter Hartz directed a governmental commission which submitted in 2002 a plethora of reform proposals. They should help to overcome the unbearably high unemployment rate of more than 10% in the whole country, up to officially 25 % of the entire working population in some areas of eastern Germany. Many of these reform ideas had been taken over from other countries – predominantly from the Netherlands, Denmark and the United Kingdom. In the context of the European Employment Strategy they were identified as “good practices”.

Summarising the 2003/4 re-enactments of social protection for the unemployed in Germany, the far reaching changes encompassed the main elements of unemployment protection: the organisation, the relationship between the unemployed and the administration, the leading principles of protection and the main instruments of placement and integration. In this respect one might say: the Hartz commission's reform proposals implemented a contractual approach to tackle with the challenge of unemployment.¹ Since this period job seeker's agreements play a pivotal role to outline strategies for the unemployed on how to re-integrate themselves into the labour market.

The reforms were inspired by the ideal of an activating welfare state, which is conceived as a means for self help to all of those who risk social exclusion. The chapter gives at first an overview on the changes implemented in the last legislative period between the years 2002 to 2005, afterwards it illustrates the achievements of the reform and, finally, it tries to answer the question on whether the reform can be assessed as a dismantling of welfare or a new version of the welfare state.

This chapter tries to illustrate the main targets and changes made in order to pursue an in-depth reform of the unemployment protection of Germany. It sketches the main reform steps (II) and tries to inquiry, to which extent the changes had been inspired by initiatives of other EU countries or had been formally approved as a good practice in the context of the European Employment Strategy (III).

¹ Els Sol/Mies Westerveld (Eds.), *Contractualism in Employment Services*, Kluwer Law International, 2005.

Outlines of the Reform

Mandate of the Reform Commission

In February 2002, a governmental commission had been nominated to make proposals on “Modern Services for the Labour Market”². The commission had 15 members, among them managers, trade unionists, politicians and academics. The chair had been taken by Peter Hartz. This manager had made a series of unconventional alterations and arrangements becoming effective in the Volkswagen Company, in order to conserve the once substantially jeopardized jobs. The commission’s proposals were addressed to the public; their main emphasis was put on the reduction of unemployment and the reorganisation of the German employment service.

The commission’s formation was the political reaction towards a scandal in the employment service, which had been unveiled by the press. It turned out that an employee in a local employment office for years whitewashed his figures on placements induced by him- without any notice taken by other instances of the employment service. This scandal indicated evident shortcomings in the monitoring and effectiveness of the German employment service. Additionally, immediately after the New Economy hype came to an end in late 2000, the figures on the unemployment rate rose substantially. The official doctrine of the government as to combat poverty was “to enhance and to demand” (Fördern und Fordern!) a modern version of a carrot and stick policy. The financial subsidies to the unemployed are granted to make them seeking work in the labour market successfully; so, all help is to be combined with the demand for a successful re-entry into the labour market. The imminent Federal Election’s date in late September 2002 gave a further momentum for the government, to issue new proposals to solve the most ponderous problem of the German internal policy of these years till nowadays– the high rate of unemployment.

Main topics of Interest

Competition in Placement

The reform commission raised the question on how a quick, effective and sustainable integration of the unemployed into the labour market can be achieved. It articulated the assumption that both the unemployment insurance and assistance and above all the placement of job seekers should be reorganised profoundly. Placement should be made more flexible, accountable and effective. The leading idea behind the reform of placement was to give competition between public and private placement agencies the broadest room ever. This should bring about a more client-oriented employment service. The reform intended to replace the bureaucratic ori-

² Bericht der Kommission, *Moderne Dienstleistungen am Arbeitsmarkt*, Berlin 2002.

entation, still prevailing in employment service by an entrepreneurial approach: The heads of the organisations should no longer be appointed as public functionaries on the basis of a lifelong tenure, but work on the basis of a temporal work contract as managers - i. e. higher paid than their predecessors. In order to put a much greater emphasis on competition in placement services, a free access to placement services should be given ; additionally, the public employment service should be made mandatory to issue vouchers for private placement services, if those were unable to find a job for the unemployed within a reasonable period of time (3- 6 months) . The main task of placement services should be the acquisition of jobs and job seekers and not the administration of unemployment benefits. Benchmarking and quality assessments and also competitions between the various local entities of employment services within the employment service should create a general climate committed to overcome the unemployment by improved endeavours to placement in as many respects as possible. The benefit should not pamper the recipient to stay unemployed, but be frugal enough to give an incentive to take over also badly paid work.

Structural reforms in unemployment insurance

Additionally, the reform commission listed a whole series of structural changes of the unemployment insurance scheme. The leading motivation, upon which the proposals were brought forward, was summarised in the saying: “induce initiative – safeguard security!” (Eigeninitiative auslösen - Sicherheit einlösen!). This maxim illustrated the activating strand the labour market reform proposals of the commission were built upon. The process of labour market integration should be accompanied by consultation, support and financial protection. The local employment services – traditionally called “Arbeitsamt” (work office) – should be called with the artificial American word: “JobCenter “.

Each of these entities should dispose of a budget on its own discretion out of which it should finance the appropriate instruments for integration. The reform should coax the local employment offices to spend the main in the most effective and appropriate manner, based on the discretion of the local entities without any interference of the federal or regional authorities. In the long run, the unemployment insurance – till restricted to dependent workers – should be transformed into an income protection system for both wage earners and the self-employed. The new centres should not only focus on placement and re-integration of the job seeker into the labour market, but also assist the individual in the plethora of social hardships and handicaps of the unemployed persons by rendering services and assistance as to their health, drug, sanitary, addiction, debt, housing or education problems. All social work activities should be concentrated in the job centres. Within these centres, however, the placement work should be separated from the other activities of social work. The latter should be devoted to special services which should densely collaborate with other services of the centre.

Placement should be made effective as quickly as possible. So, both employee and employer should be imposed the commitment to indicate a job vacancy as fast as possible. Each violation of this commitment should be sanctioned severely. The criteria for job offers should be enlarged in the sense – that for each job seeker each lawful and adequately – i. e. in line with the existing collective agreements – paid should be acceptable. In the formation and definition of the re-integrative strategy an integration agreement should play the key role. This should be elaborated by the case manager of the centre and the job seeker and figure out the strategies to be carried out by the job seeker in order to regain a paid work.

Further proposals for changes were addressed to unemployed persons over 55 years or physically or mentally handicapped persons. For them work should be found on the basis of contacts for services concluded between the job centre and an employer, who not become the employer of the unemployed, but should hire their services on a contract concluded between the employment administration and the employer. In the contract the price for hiring the unemployed temporarily should be fixed. Unemployed should also be empowered to start their own business by utilizing their beneficiaries' rights to temporal income support and social protection also while earning at the commencement of their work a small income as a self-employed.

Merging two systems of assistance to one

Before the reform had taken place unemployed persons, who exhausted their beneficiaries' rights under the unemployment insurance scheme were entitled to a means tested benefit, if they – as regularly - did not dispose of substantial means of their own to afford their adequate living. In case of unemployment there were two competing systems of means tested benefits: the unemployment assistance (Arbeitslosenhilfe) and the social assistance (Sozialhilfe). For those who got unemployment insurance benefits before the assistance did not depend on needs but on the previous income of the unemployed. For the unemployed who were not covered by the unemployment insurance immediately before becoming dependent they received a benefit, which was determined according to the need of the unemployed individual and her/ his family. This duplicity of assistance schemes lead to inconsistencies, contradictions and a twofold protection. The assistance for the needy unemployed was too complex to be conserved. So, the ultimate proposal of the reform commission was to merge the two systems and make a unique scheme out of it.

Making Hartz Reform Work

Not all, but most of the proposals were implemented by four legislative acts. In the public debate they were abbreviated as "Hartz I to Hartz IV". Each piece of legislation assumed various elements of the reform commissions' proposal. The changes proposed had been conceived as a profound desecration of the inherited principles of the welfare state. So, the phase of legislation and implementation was accompanied by a series of protests and public manifestations - above all in high unem-

ployment areas of East Germany Monday's manifestations in remembrance of the manifestations' traditions which once brought down the East German communist regime.

Improved placement (Hartz I)

In the First Law on Modern Services on the Labour Market³ the deficits in the placement service should be altered. The employee had been made mandatory to indicate an imminent redundancy immediately after the redundancy was declared. This reform step should abbreviate the period of unemployment by implementing the job research at the most early moment possible. Additionally, an institution was established, which meanwhile was already dissolved because of lacking efficiency. The employment service should also be active as an employment business. It should not only indicate job seekers but should also offer the working capacity of unemployed persons on the basis of a contract for work. In order to fuel the efficiency of public employment services already in 2002 the instrument of placement vouchers had been introduced⁴; in 2003 this instrument had been enlarged as to training services. In order to strengthen the market mechanism and to empower the beneficiary, she or he was entitled to demand services from private training providers on the costs of the public employment service.

Part-time work, self-employment and household work(Hartz II)

The Second Law on Modern Services on the Labour Market came into force at January, 1st, 2003⁵. It made the small jobs of a low monthly income more attractive by lowering the overhead for taxes and social contributions to 25 %. To combat moon light work in households a tax-deduction for housekeepers' wages had been implemented. And finally, unemployed persons can receive subsidies when starting their own business. Both initiatives became a success both the so called "mini-jobs"- so the official "German" word – as the support given to persons keen on starting their own business had been accepted by many unemployed persons.

Restructuring employment service (Hartz III)

The Third Law on Modern Services on the Labour Market⁶ became effective on January 1st, 2004. It reorganised the more than ninety thousand employees in six hundred offices of the Germany wide operating unemployment and placement office "Bundesanstalt für Arbeit" into a more service oriented agency. It is from that time onwards called "Bundesagentur für Arbeit". This change from "Anstalt" -

³ of December 23, 2002, BGBl. I S.4607 BT-Drucksache 15/25.

⁴ Regina Konle-Seidl, New Delivery Forms in Germany, in Els Sol/ Mies Westerveld (Eds), Contractualism in employment services, Kluwer Law International 2005,187, 190 ; Oliver Bruttel, New Private Delivery Arrangements in Germany, *ibid.*, 209, 222.

⁵ BT-Drucksache 15/26.

⁶ BT-Drucksache 15/11515.

which reminds to a state institution - into an agency, which sounds like a private enterprise should symbolise the conceptual change of this enormous administration. The changes brought about a new logo, a new approach towards utilising the internet and other communication services to improve the cooperation between the employment agencies and the beneficiaries, which had since then be called “clients”. The contract management within the organisation had been implemented. A reduction of the ratio between case-mangers and beneficiaries was intended in order to reduce the efficiency of placement.

Merging two systems of assistance for able-bodied (Hartz IV)

As the most profound change was conceived the Fourth Law on Modern Services on the Labour Market⁷, meant to reorganise the financial support of those unemployed persons, who have exhausted their benefits rights. The traditional division between unemployment assistance and social aid had been replaced by a new system in 2005. After the reform the assistance scheme had been transformed on drawing a new – but in the history of social policy a quite old distinction⁸ – between the able-bodied and those needy persons being incapable to do gainful work. The first piece of legislation was incorporated in Social Code (Sozialgesetzbuch) II, the latter in Social Code XII. The first is financed predominantly by the national budget, the latter by the municipalities.

So, systematically spoken, the “merging” of unemployment assistance and social assistance did not touch the duplicity of assistance schemes in Germany, but brought about a new borderline between two still existing schemes. The limit is based upon the traditional distinction between the non work-able and the work-able poor – a borderline, which was in quite old days conceived as the frontier between the deserving and the non- deserving poor.

The new law made necessary to find a solution on the administrative responsibility. Two proposals had been made – one was to make the employment service responsible also as to the social services for the many handicaps and short comings of the unemployed persons. The other proposal was to make the municipalities, originally competent to administer social assistance benefits – also to act as a part of the employment service. The law provides for the general competence of the employment office; but 69 municipalities got the right to administer the whole new scheme by their own administrations. Till 2011 the final assessment shall be made based on the experiences of the competing organisations. Already today, however, it is obvious, that the employment service, which has to collaborate with the various social services of the municipalities is not an appropriate organisation, because the limits of action are not clear cut and the direction of such a unit turned out to

⁷ BT-Drucksache 15/1516; Eberhard Eichenhofer, Sozialrecht, 2007 (6. Aufl.), Tübingen, Textziffer 482; Johannes Münder (Hg.), Sozialgesetzbuch II, Grundsicherung für Arbeitsuchende, Baden-Baden 2007 (2. Aufl.); Herbert Renn/Dietrich Schoch (Hg.), Grundsicherung für Arbeitsuchende (SGB II), Baden-Baden 2007 (2. Aufl.).

⁸ Eberhard Eichenhofer, Geschichte des Sozialstaats in Europa, München 2007, S. 38 ff.

become extremely complex, because of the lack of a transparent internal organisation⁹.

The law brought a redefinition of the elementary needs. The payments monthly transferred to the recipient were increased for 16% compared to the previous legislation on social assistance. On the other hand, single benefits to meet single needs (winter coat, heating materials, school meals or excursions, TV set) were now longer paid by social assistance. For the recipients of the former unemployment assistance the change mattered deeply because the former system was income based. So, the unemployed persons, who had lost a well previous paid job, lost more than those with lower incomes out of paid work. Under the new scheme all recipients are integrated into the social insurance to protect them in cases of old age, invalidity and sickness. The protection as to pension rights, however, is definitely modest. This is due to the expenses necessary for the acquisition of protection under the German pension scheme. So, for one year of unemployment benefits' receipt a pension right matures, which gives an entitlement for 4 € (from 2007 onwards only 2, 15 €). This is definitely low, because an ordinary worker earns with work paid on the average basis a pension right of over 25 € a year. So from one year of subsistence payments matures a pension right of less than one month of a worker who earns an average income.

The new assistance scheme for the needy unemployed persons introduced a series of unprecedented elements. The benefit is defined upon a family unit (*Bedarfsgemeinschaft*); it encompasses all needy family members, irrespective of their legal status. They count as a unit of both need and as resources. Also in the absence of legal maintenance obligations – so among unmarried couples – they deemed to support one another. In this construction a potential for increasing benefit rights by restructuring one's family life opened space for unexpected effects on increasing the number of family units and, hence, the amount of cash transfers, e. g. parents once lived with their children in a flat rented a part of their flat to their children. So they were conceived as a family unit of their own with an entitlement to further benefit rights¹⁰.

The beneficiary with working potential is obliged to contribute actively to her/his integration into the labour market. Each one has to agree on an integration agreement (*Eingliederungsvereinbarung*), which has to determine the ways and means pursued by the unemployed to achieve re-integration into the labour market. This change coincides with an alteration in the understanding of reasonable alternative employment¹¹. The formerly respected right of being acknowledged as employable on fields of activity, on which the individual has proven to be skilled by her/his previous occupation had been altered by the new rule: each unemployed

⁹ Ombudsrat. Grundsicherung für Arbeitsuchende Schlussbericht Berlin 23.6.2006; The Federal Constitutional declared in late 2007 this construction based on an integrated administration of federal and local entities as unconstitutional.

¹⁰ Ombudsrat, Grundsicherung für Arbeitsuchende, Schlussbereich, Berlin 23.6.2006.

¹¹ Ingwer Ebsen, Contracting Between Social Services and their Clients in the German Concept of *Fördern und Fordern*, in Sol/Westerveld, 231, 241.

person is expected to pursue each lawful and lawfully paid occupation available on the labour market. The contract notion points out that under the law of unemployment protection a reconciliation between the beneficiary and the administration takes place, which might correct and limit the wide scope of optional occupations – assessed to be reasonable by law - what occupation is appropriate is not primarily a matter of general principles but is to be specified under the very concrete auspices of matching on the local labour market¹². Integration of the unemployed persons aged under 25 years became imperative.

The benefit is given as a subsidy and understood as a basic income (“Grundsicherung”), payable in lack of other support, above all on the basis of a work contract or an unemployment insurance entitlement. It is based upon the assumption, that member of the family, which do not belong to the household of the beneficiary are not mandatory to support the unemployed, e. g. the children of the elderly unemployed persons. The federal budget covers the cost for the living allowance and the contributions for the unemployed to their pension and health insurance; the costs for housing are borne by the municipality of the place of residence. A subtle debate emerged on how to deal with income earned as a beneficiary. The law provided for a partial reduction of the benefit in case of income reception: 15 % of an earned income till 400 € 30 % of an income between 401 € and 900 € and 15% of an income of more than 900€ a month remained free of deduction. These percentages and limits were highly controversial. Critics argued the high deduction would act as a disincentive to reintegration into the labour market. However, if the deduction would be less restrictive, the whole system would attract to many persons to become unemployed. This example shows clearly, that the incentive structure of unemployment protection schemes can be analysed under different angles. At the moment, once again a revision is in the making, directed towards making small extra- incomes becoming more deductible than before to avoid that unemployed stick too long and to frequently at the state of unemployment and by reducing higher extra-incomes less than before in order to make the take-over of extra- work more attractive

A further highly controversial issue related to additional public work which is offered to those unemployed persons who are not likely to get a job on the labour market easily or even at all. They can do public work for an additional remuneration of 1€ per hour. So, these opportunities were called “1 € jobs”(German: Ein Euro-Job). They offer income for non marketable services. The political debate focussed on whether it could be fair “to offer jobs for such a low salary”. The critics did not take into account, that these jobs are not meant for being done on the labour market, so that those workers would and should not compete with regularly paid workers, who do earn at least 4- 5 € an hour. Additionally, the critics are not aware of the fact that the basic needs are met by the social benefit, so that the 1€ job brings extra money which is to be added to the benefit covering the elementary needs.

¹² Ebsen, 245.

Good practices of other countries – dubious practices in Germany?

Reform fits into the European Employment Strategy

For the framers of the reform the European Employment Strategy and examples given by other EU member states were taken into account. This intention was quite often and explicitly articulated in the reform process¹³. So, all the suggestions were understood as authentic interpretation and conclusion from the European Employment Policy Guidelines on which the EU and the member states agreed upon in the framework of the European Employment Strategy. The lesson one can draw from the German reform experience already after a while is : the labour market is divided into those persons who are adequately – above all intellectually – qualified, and who quite normally do find a suitable occupation after having been unemployed beforehand, and of those, who do not dispose over sufficient qualifications. They have severe handicaps to regain a job at all, because the labour market – with its high costs imposed on labour – is not open for the creation of low skill jobs, which allows the employee to acquire a still decent income out of work – above all an income which exceeds the income from social benefits¹⁴. In these days, the German public realizes more than ever of being challenged by an increasingly growing low income population living at the brink of social exclusion. Above all in the high employment regions of East Germany a growing part of the population is jeopardized by sinking prospects in an ever possible future re-integration into the labour market.

Examples for good practices

So, in some of the proposals examples given by other member states can be discovered quite easily. The organisational reform drew many lessons from the Dutch reform on *werk boven incomst*. Also the *contrat d'insertion* of France and the British Job seeker's Agreements gave a sort of blueprint for the integration agreement. The measures taken to integrate those under 25 years have strong resemblances with the British New Deal approach and the Danish emphasis on facilitating the unemployed person with training and other efforts to increase their employability, also these traces can be detected in the proposals made and submitted. As the examples quoted the German reform put more power of discretion to the employment administration. In this respect the reforms marked an end on the bureaucratic and authoritarian traditions still prevalent in the German employment service and replace

¹³ Bericht p. 20, 341 et sequ.; look also Bruno Caruso/Maximilian Fuchs (eds.), *Labour Law and Flexibility in Europe – The Cases of Germany and Italy*, Baden-Baden/Milano 2004; Christian C. Steinle, *Europäische Beschäftigungspolitik*, Berlin 2001.

¹⁴ Ombudsrat, *Grundsicherung für Arbeitsuchende*, Schlussbericht, Berlin 23.6.2006.

this model by a more managerial approach. This change had been appreciated by both the personnel as the clients. But it is dubious on whether it is more than a model of conduct and became indeed a part of reality.

Tough reconstructions?

Because of the profound changes – above all the ones made in the context of reforming the assistance to the unemployed - there was a massive uproar against this reform – above all in the East German regions, where poverty and unemployment are most spread. There the main argument was the reform ends in a drastic cut back of benefits.

After some years, after the reform got traction, it turned out, that the new system is more costly to the public than the previous one. The protest of the period of debate and deliberation reverberated: What was criticized once as the most drastic social cutback ever, turned out to be much more expensive than the previous system had been ever! So, this experience ushered in new questions, stemming from the opposite side of the political spectrum. The question is raised: Is the scheme too generous? Is it more attractive than ever? Should more emphasis to be given to a combination of income from social transfer and work by restructuring the rules on deducting social transfers for those earning small amounts of work income? Predominantly, the increase is due to an unexpected increase of beneficiaries. This might be the consequence of definitely unfavourable conditions on the labour market, an increasing tendency of persisting, long term unemployment and the making public of poverty, which had been hidden in the past. In any respect, if one should characterise the reforms made in Germany during the last years in the system of unemployment protection one could not assess it as a series of cutbacks, but it can be more precisely understood as a means to put Germany in line with the European development – above all of those member states who changed their system of protection most profoundly in the direction of the activating welfare administration. Also under a social perspective the lessons from Germany might attract attention outside this country: because the consequences of the German reform process can show, that an activation policy is embedded in social circumstances – which are not alike in all countries and parts or regions of country due to remarkable social and economic differences : matching on the labour market is easier under low unemployment rates, however far from effective at all, if the unemployment rate is so enormous, that there are more unemployed than employed persons. Different activation models, hence, react differently, when they are established and embedded in different economic environments and under distinct social circumstances.

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