

Discussion paper

EUROPEAN EMPLOYMENT OBSERVATORY

Flexicurity in Germany

by

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1. Defence of standard working contracts

A flexicurity approach similar to the Dutch or Danish system does not exist in Germany. Labour law regards the regular working contract (*Normalarbeitsverhältnis*), which includes full-time work on a perpetual basis, as the norm. Also the majority of the population takes this kind of contract as a benchmark. Trade unions were sceptical about the introduction of flexible forms of employment, like part-time or fixed-term contracts, and they objected the deregulation of redundancy laws. Under these conditions, companies developed a two-sided strategy promoting internal flexibility of the core staff on one hand and using flexible working forms of employment for peripheral tasks on the other. The government finally took responsibility for the income support of those who could not successfully compete under these labour market conditions. More, than in many other European countries, the German labour market is segmented between owners of core jobs, peripheral workers and the unemployed.

The main reason for this approach is the preference for labour efficiency which is seen as a decisive determinant of economic growth and competitiveness of the German industry ([Vogler-Ludwig 2004](#)). Many policy approaches, therefore, targeted at raising the productivity of existing working places rather than extending their number. This was achieved through capital investment, promotion of research and development, and training of workers. The decline of labour demand was more or less seen as a secular trend which could hardly be changed. "The end of labour" became a prominent idea.

Gradually, however, labour market policies changed during the 1990's towards greater flexibility. Part-time employment increased considerably together with self-employment and other flexible forms of jobs. The limitations of the prevailing policy approach became evident: protective labour law has had a high price in terms of unemployment, and working time reductions at existing working places did not create a sufficient number of jobs.

Under these conditions, labour market policy developed various elements of the flexicurity which targeted at stabilising existing jobs rather than raising external mobility. During the last two decades labour market flexibility was extended and restricted on changeful paths.

2. Major flexicurity instruments

Nevertheless, a variety of flexicurity elements can be discerned in Germany. Based on the Hartz reform, active labour market policy developed several bridging systems. In a wider sense of flexicurity, Germany improved labour market flexibility without reducing the comparatively high levels of social benefits. In particular, these flexibility measures were:

- The Job Promotion Act (*Beschäftigungsförderungsgesetz*) from 1985 which allowed fixed-term contracts without the former activity-related restrictions. In 1996 the duration of fixed-term contracts was extended to 24 months, and activity-related restrictions were introduced again in 2001. Surprisingly to both advocates and antagonists of flexibility, the rise of fixed-term contracts was rather limited. The share of fixed-term contracts grew from 5 % in 1985 to 7 % in 2003. However, among young workers (< 25) the increase was significant. This observation was the reason for the actual governmental plans to extend probationary periods of job entrants and restrict fixed-term contracts.
- Redundancy regulations were also reformed by the Job Promotion Act and by further steps, excluding small businesses with less than 25 employees from the regulation. However, dismissals regulations are still seen as a cumbersome instrument to adjusting labour input, as the legal demands for dismissals are high and the selection of workers is restricted by various group-specific protection rules (Hanau 2005). Reform proposals are, therefore, still in the debate among the coalition parties.
- The current proposal made by the Federal Minister of Economics and Technology (Glos) seeks to combine both labour market flexibility and the increase of unemployment benefit. This suggestion follows the Danish model of flexicurity.
- The major steps to liberalise agency work go back to the 1985 reform. Based on the theory of transitional labour markets agency work was then introduced by the Hartz reform as public Personnel Services Agency (PSA) which should place unemployed workers.
- After changes from liberal to restrictive and back to liberal regulations, the number of minor jobs grew rapidly and regular registered employment decreased. The Mini-Job-Regulation of 2002 regarding jobs with incomes up to EUR 400 per month also increased the number of jobs in this area up to 4.6 million. Even though there is no direct link between the growth of mini-jobs and the decline of registered employment, it indicates a fundamental change of employment conditions on the German labour market.

The following presentation will concentrate on measures of greater importance:

- Short-time work (*Kurzarbeit*) has existed for decades. It supports jobs in companies with temporary sales and production slumps through benefits according to unemployment insurance.
- The market for temporary work (*Zeitarbeit*) expanded considerably during the last two decades. In addition, temporary work became part of the Hartz reform through public Personnel Service Agency (PSA) which tried to place unemployed workers in regular employment.
- The instrument of transfer companies (*Transfergesellschaften*) was created which supports workers discharged in the course of company closures by providing extended unemployment benefits, placement and training measures. Under German law this is called the structural short-time scheme (*strukturelle Kurzarbeit*).
- Collective agreements started to include opening clauses for wages and working times in exchange for job guarantees on the company level.

2.1. Short-term work

In the case of temporary production shortfalls companies can apply for short-time benefits for workers. This is regulated by Social Code III (§§ 169).

The approval of short-time benefits depends on several conditions:

- A considerable part of working time cannot be used by the company productively; at least one third of the workers will have to work 10 % less than normal.
- The slump in labour demand is temporary and there are founded expectations that the situation will improve in the future.
- The working time reduction is unavoidable and the works council agrees.

In this case workers receive 60 % of the net wage for lost working hours (67 % for workers with one child). Normally the benefit is terminated within six months. Exceptions are allowed up to 24 months. In this case workers can be placed in other companies by the labour offices.

During the cyclical crises in Western Germany during 1975, 1983 and 1994 up to 1% of the total volume of working hours was covered by short-time work. 300,000 short-time workers were counted at maximum. In Eastern Germany short-time work was used during the initial transition phase after the Germany unification. 1.5 million workers were supported at that time. This reveals that short-time work effectively stabilised jobs in the case of economic crises. The strong correlation with the business cycle also indicates the temporary use of the instrument.

After 2000, short-time work did not react in the same way as before. The share of short-time working hours remained at the level of 0.2 %. This can be explained by the dominance of structural trends on the German labour market, leading to a long-term stagnation of labour demand. Moreover, since 1989 employers have to pay full social contribution rates for short-time workers. This made short-time work more expensive for companies. Finally, the introduction of working-time accounts in many companies helped to adjust working hours over longer periods of time (IAB 2005, pp 176).

2.2. Agency work

One of the important flexicurity instruments in Germany is agency work which has been practiced for more than 30 years. The temporary work agencies sector continued to grow until recently.

The legal basis for agency work is the Temporary Employment Agency Work Act from 1972 with a series of updates – the last in 2003 (*Arbeitnehmerüberlassungsgesetz*). The regulation targets the protection of temporary workers, prohibiting illegal practices and defining the borderline to private placement services.

Temporary work agencies have to be approved by the Federal Labour Agency. This approval requires the reliability of the agency, in particular regarding the payment of social contributions, taxes, and the compliance to occupational health standards. Temporary work in the construction sector is linked to the existence of a mandatory collective agreement covering non-sector-related agencies. Such a collective agreement, however, was not concluded. This means that non-sector-related temporary work agencies for the construction sector do not exist.

Temporary work agencies conclude labour contracts which follow regular standards regarding wages, holidays, sickness payments etc. Labour conditions are regulated through collective agreements for agency work. Alternatively labour conditions can be equivalent to comparable employees in the hiring company. This includes remuneration. Agency workers have the right to be informed about equivalent working conditions. The duration of agency work is unlimited. Fixed-term contracts are generally not allowed, except if the worker has good reasons to conclude such a contract. The maximum period for fixed-term contracts is 2 years.

The temporary work agency enters a contractual relation to the hiring company while borrowed workers remain associated to the agency. Wages have to be paid for the duration of the contract rather than the employment in the hiring company. The agency is obliged to pay taxes and social contributions, and it has to guarantee health standards to their employees. The hiring company has a subsidiary liability for the payment of taxes and social insurance rates.

The Hartz reform (Hartz I) introduced public Personnel Service Agencies (PSA) which were established by the labour offices. These agencies should place unemployed persons in companies, in particular those unemployed who had difficulties in finding a job but were not promoted through other measures.

The total number of approved temporary work agencies was 11,953 in 2004. 46 % of agencies received an unlimited approval. Around 1,500 approvals were withdrawn during the year. The number of agency workers increased from 328,000 in 2000 to 453,000 in 2005. Agency work is characterised by substantial seasonal fluctuation. One third of agency workers are female. About one sixth are foreigners.

43 % of agency workers in 2003 came from unemployment but only 34 % were unemployed after finishing agency work (Antoni, Jahn 2006). This indicates a positive employment effect among the group of agency workers. The presence in the labour market demands the company provides the opportunity to demonstrate the efficiency of work. The “adhesive effect” of agency work however, is decreasing in recent years.

The duration of agency work is rather short. Almost all of the contracts are terminated within one year. 58 % lasted less than three months. The median employment period was 2.1 months in 2003.

The largest group among agency workers were unskilled blue collar workers (37 %), and skilled manufacturing workers (28 %). While the use of unskilled agency workers increased by 25 % between 2000 and 2004, the demand for manufacturing occupations stagnated. Administrative work even decreased by 3 %. The growth areas were technical and service occupations.

Agency work in Germany covers parts of the “spot labour market” providing short-term engagements in labour demanding companies. In addition it leads to job placements in the hiring companies. Thus it is part of the transitional labour market contributing to more stable employment, at least to some extent. Agency work itself however, does not provide stable employment as most of the jobs are short-term. The security providing part is largely played by unemployment insurance. Recent labour market reforms contributed to this development as multiple entries into agencies are now allowed.

2.3. Transfer companies

The massive outplacement from eastern German companies after unification brought the idea of transfer workers to job creation companies (*Beschäftigungsgesellschaften*) which provided both job security and training during the transition phase. In parallel, the instrument of “structural short-time work” was used mainly in western Germany to reduce labour market risks of company closures. The development was strongly influenced by the theory of transitional labour markets which draws particular attention to the periods of change in individual employment careers and demands for public support during these phases. While short-time work absorbed cyclical changes of employment, the new approach addressed the decline of companies and sectors. The instrument is focussing on training and retraining of workers at risk. Transfer short-time work, as it has been called

since the Hartz reform, should raise the flexibility of labour by reducing labour market risks. Thus it is a typical flexicurity instrument.

The existence of transfer-companies is based on two legal principals that are included in the dismissals act in form of the regulation of redundancy payments in the case of mass redundancies and the provision of transfer benefits in the Social Code III:

- Following the dismissals act (*Kündigungsschutzgesetz, § 17*) all dismissals of more than 30 persons within 30 days have to be announced to the local labour agency and the works council of the firm. The works council has the right to negotiate on the dismissals with the employer and to take action to avoid it or reduce negative consequences. A “social plan” (*Sozialplan*) should compensate the disadvantages for workers resulting from the changes. This plan has to regulate redundancy payments, the remuneration of relocations and training costs and other issues.
- Transfer benefits (*Transfer-Kurzarbeitergeld, SGB III § 216b*) are provided to employees affected by the closure of businesses. Two types of payments exist: *transfer measures*, which help to re-integrate employees in the primary labour market. These measures are subsidised with 50 % of total costs and the maximum of EUR 2,500. *Transfer benefits*, which are paid for the maximum period of 12 months; the level of payment is 60 to 67% of former net wages as in the case of regular unemployment benefits. The precondition for this type of benefits is that the workers affected by company closure are brought together in a self-contained transfer company (*Transfergesellschaft*). All workers have to pass a placement assessment (profiling) which helps to forecast their placement probability.

These regulations involve three parties for the funding of mass redundancies:

- the employers have to pay redundancy compensations based on individual and social criteria,
- public unemployment insurance supports the transition phase through the transfer benefits,
- employees disclaim on parts of their net incomes.

Based on these instruments, an extensive outplacement business grew in Germany. Big companies and the HR consulting business developed the transfer-company to one of the major restructuring instruments in the course of the rapid decline in manufacturing employment. The most comprehensive instrument of outplacement is the transfer company (*Transfergesellschaft*). This is based on the foundation of a follow-up company taking over the staff of a business which will be closed. Using unemployment benefits and other public transition subsidies, the transfer company guarantees incomes for a limited period and provides outplacement services to the staff.

Workers generally receive 80 % of their former net income in general. This consists of 60 to 67 % from transition benefits paid by the Federal Labour Office. In addition, employers have to pay for an add-on wage (13 to 20 %) to achieve the 80 % level, social contribution rates, training costs, and the administration of the transfer company. These elements sum up to 50 % of the former labour costs. In many cases this is co-financed in exchange of shorter periods of notice and lower redundancy payments.

The application of transfer short-time work rapidly increased with the new regulation in 1998. In 2004 the number of business locations using the instrument was 3.6 times higher than in 1998. The number of workers included in the measure more than doubled during this period. In 2004 the share of transfer short-time work among all business locations using short-time schemes was 8.4 % in western Germany. Following the G.I.B. statistics for North-Rhine Westphalia, the instrument of transfer short-time work is strongly used by large companies. The majority of workers in transfer companies is over 50 years (53 %), and 82 % are men. Thus the staff structure in North-Rhine Westphalia strongly concentrates on the difficult targets groups of the labour market.

2.4. Opening clauses in collective agreements

Facing the erosion of the system of collective bargaining, many sectoral trade unions are confronted with strong demands for more flexible agreements. In general the need for greater flexibility is justified with increasing competition on product markets and the expected loss of jobs. Therefore, greater flexibility of wages and working hours is often compensated by job-stabilisation agreements (company-based employment pacts) which guarantee jobs for the near future. Following the works council survey of the trade union institute WSI, (*Wirtschafts- und Sozialwissenschaftliches Institut des deutschen Gewerkschaftsbundes*) among 2007 works councils in companies with more than 20 employees, 25 % of German companies established company-based employment pacts, 55 % among those with poor economic performance and 20 % among companies with a good performance. The pacts are valid for 19 months in weak companies and up to 3 years in stronger ones.

The opening clauses of these agreements in general allow deviations from collective agreements for a limited period of time, in most cases with the approval of the social partners. Early agreements of the 1990's required evidence for severe economic hardship (for example, the company is closed to bankruptcy). Present opening clauses can be used to improve competitiveness. They are now also accepted for the purpose of defending jobs at the location.

3. Understanding of the flexicurity approach¹

With regard to the upcoming debate on flexicurity, the Federal Ministry of Labour and Social Affairs (BMAS) urges for a context-related and institution-based interpretation of flexicurity. Officials point to the differences between Denmark or the Netherlands and Germany. In particular they refer not only to the size but also to the different social systems, different political cultures and in particular, to the differing public attitudes towards flexibility and social security. Following the official arguments, the Danish model can hardly be taken as a hardcopy for German reforms. Nevertheless, the German government supports the European social model which combines flexibility with social security² and points to a series of steps to increase labour market flexibility.

The German approach was and is to improve internal flexibility within companies by providing training and reducing functional barriers but restricting external flexibility. It is job related rather than labour market related flexicurity which is seen as the superior answer to changes in market conditions. Therefore labour market reforms "should not abandon internal solutions in an over-hastily way" (*BMAS official*).

Officials also argue that there is a certain discomfort with the flexicurity approach. In particular they worry that the extension of labour flexibility could release employers from their responsibility to secure jobs and to share the costs of adjustment. They emphasise the necessity that employers also keep employees during phases of cyclical downturns. Company-based solutions should be found and social partners involved. "A new balance between flexibility and security will have to be found which includes the commitment to solidarity." (*BMAS official*).

¹ Based on interviews with BMAS officials. Governmental documents are not yet available.

² As the coalition treaty states: "Das Europäische Sozialmodell als Bestandteil der Lissabon-Strategie muss weiterentwickelt werden. Dabei wird es für die Bürgerinnen und Bürger ganz entscheidend darauf ankommen, dass es gelingt, die notwendige Flexibilität mit sozialem Schutz und sozialer Sicherheit zu verbinden ("Flexicurity")."

Moreover, a series of disadvantages are perceived in the flexicurity concept:

- high transaction costs related to external flexibility in particular in form of retraining workers
- rising risks of precariousness for disadvantaged groups of workers
- declining training investments by employers and workers due to shorter employment prospects
- high public cost of generous unemployment benefits and training systems

Thus, flexicurity is discussed in the context of combating illegal employment and precarious jobs, searching for more social security in these areas.

Furthermore German labour courts disapproved flexibility in dubious cases (Hanau 2005), and the trade-union-oriented publication by the Hans-Böckler-Stiftung states that "... the coordination of social life cannot and must not be put into the hands of markets, least of all if the social organisation of work is considered. ... Market flexibility is only possible within the social boundaries." (Kronauer, Linne, 2005, 13).

4. Chances for a flexicurity approach

The recent policy reforms did not really succeed in substantially easing labour market transition. The segmentation lines between the insecure employment sector and what is regarded as "regular" or "standard" employment, were not removed. The divide between external and internal labour markets is still important.

However a considerable increase of flexibility can be observed among employers and workers trade unions in particular:

- Flexible working-time schemes were introduced into collective agreements allowing for wider variations of individual working hours over the year. Regular working hours were also adjusted by collective agreements in exchange for a few years of job guarantees. Moreover, opening clauses were negotiated and signed in various branches, which allow vulnerable companies to pay less than collective wages during crises.
- Companies are developing models to increase the internal flexibility in case of industrial restructuring. One example for this is the creation of internal outplacement and temporary work agencies by some large companies.
- Workers increasingly used flexible forms of employment. The number of part-time jobs, self-employment and marginal jobs grew considerably in recent years.

A flexicurity-orientated reform, which follows the Danish model, would nevertheless undermine fundamental principles of the labour market constitution in Germany.

First of all, employment protection through redundancy regulations and work councils would have to be abandoned. These, however, are core elements of labour law and co-determination. Principal changes would not be possible without compensation of workers in the form of (very) favourable job opportunities on the German labour market or generous unemployment benefits. Regarding the labour market and the budgetary situation in Germany, both alternatives appear to be rather unfeasible.

Secondly, an efficient training and re-training system would be required which concentrates on life-long learning rather than initial vocational training as is currently practiced in Germany. However, employers are supposed to reduce their training investments if poaching becomes a more severe problem. This would be the case in a labour market where flexibility rather than continuity is the norm. Therefore, individuals and public budgets would have to bear more of the cost burdens.

Thirdly, changing a job would involve very high risks as workers lose a relatively high level of legal and real job protection in exchange of a more or less unprotected job – at least during the qualifying period. Just recently, this qualifying period was extended to 24 months and employment protection in small companies or new businesses does not exist at all. This is a fundamental reason for low labour market flexibility in Germany. Therefore an uneven distribution of labour market risk can be discerned on the German labour market. The dominating but slowly declining area of “normal jobs” (*Normalarbeitsverhältnis*) which have a high level of protection through redundancy regulations and representation by works councils is now surrounded by a growing area of minor jobs, self-employment, and fixed-term jobs. Nevertheless, employment stability of “standard” jobs is still relatively high in Germany.

Fourthly, the majority of the population prefers regular full-time work in an unlimited job, as the standard and legislation takes it as a norm. Discontinuity of careers as can be found for example, in the US labour market would hardly be accepted, even by companies. Thus the potential advantages of flexible working lives (learning effects in particular) get low grades. High labour market flexibility strongly contradicts with working life ideals. Unsurprisingly the reader of “Flexicurity” published by the Hans-Böckler-Stiftung, identifies many more risks than chances. The limited positive effects of recent flexibility measures contribute to this assessment.

Thus the major task of a flexicurity strategy in Germany would be to gradually raise the flexibility of regular jobs, for example, through switching from legal job protection to minimum standards for dismissals compensation. This would reduce the risks of leaving a job for a new appointment elsewhere and give clear cost relations to companies.

A second task would be to strengthen the employability of workers through extended public support of continuing training and retraining. While general training is publicly financed, large parts of dual vocational and continuing training are not. The old idea of training vouchers could contribute to the development of a training market for the needs of workers rather than companies and also include the development of standardised training certificates.

Most importantly, however, the implementation of a flexicurity strategy simultaneously requires a positive growth and employment strategy. Even if flexicurity can be associated with positive employment effects it can hardly be expected to solve the unemployment problem by itself. In a labour market where only 20 % of the unemployed have a realistic chance of getting a job, the risks of changing a job are very high. Inflexibility on the German labour market therefore, also has to be attributed to the lack of job opportunities. Consequently labour market reforms should focus on non-wage labour costs and all other cost effects of labour regulations and integrate the flexicurity approach into a wider employment growth strategy.

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