

Discussion paper

**EUROPEAN EMPLOYMENT OBSERVATORY
GERMANY**

EEO Review: Self-employment, 2010

by

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Abbreviations

BfB	Federal Association of Freelancers (<i>Bundesverband der freien Berufe</i>)
BMWi	Federal Ministry of Education and Research (<i>Bundesministerium für Wirtschaft und Technologie</i>)
DIHK	Association of German Chambers of Industry and Commerce (<i>Deutsche Industrie- und Handelskammer</i>)
IfM	Institute for Middle Class Research (<i>Institut für Mittelstandsforschung</i>)
SME	Small and medium sized enterprises
ZDH	German Crafts Association (<i>Zentralverband des Deutschen Handwerks</i>)

1. Introduction

Self-employment has a long tradition in Germany. In particular the large amount of craftsmen and the economic success of the middle class industry raised the importance of the so-called middle class policy as element of economic policy making. Several measures promote self-employment and business start-ups. In the last years the measures also comprised political instruments for the transition of unemployed to become self-employment.

In 2009 around 4.2 million people were self-employed. This equals to 11 % of the labour force. The number of persons who became self-employed in 2009 totalled to 872,000 which was an increase of 9.4 % compared to 2008. The number of new self-employed compared to people leaving self-employment was almost equal as the net amount of self-employed only slightly increased by 1.7 % in 2009 compared to 2008.¹

The high amount of promoted unemployed of new founders is remarkable. Around 20 % of all founders in 2009 were previously unemployed.² Thus promotion measures for unemployed have a strong influence on the number of business start-ups. After the introduction of the start-up grant in the course of the Hartz-reforms, the amount of business start-ups experienced a boom in 2004 and 2005. The change of the self-employment promotion – initiated by the merge of transition allowance and start-up grant into the business foundation allowance – lowered the number of start-ups from unemployment.

The financial crisis did not show the expected effects: Neither did the economic downturn lead a greater number of self-employed into insolvency nor did the minor rise in unemployment bring a further push to new foundations. Self-employment appeared as an area of stability rather than vulnerability on the labour market.

2. Assessment of nation LM policies and recovery measures

2.1. Promotion of unemployed

Self employment for unemployed is promoted by the business foundation

¹ Statistisches Bundesamt 2010

² KfW 2010

allowance (*Gründungszuschuss*) and the entry allowance (*Einstiegsgeld*). The business foundation allowance was introduced in 2006 and detached the former transition allowance (*Überbrückungsgeld*) and the start-up grant (*Existenzgründerzuschuss*) which were merged into the business foundation allowance.

Transition allowance

The transition allowance was introduced in the 80ies and supported the self-employed with the previous unemployment benefit and social insurance contributions which totalled to around 70 % of the former net income. Applicants had to submit a business plan which needed to be certified by an external institution.

Start-up grant

In the course of the Hartz reforms the start-up grant was established to promote self-employment of unemployed. The start-up grant – better known as “Me Inc” (Ich-AG) or “solo company” – comprised monthly payments of €600 in the first years, €360 in the second and €240 in the third year. The yearly income must not have exceeded €25,000. No business plan needed to be approved by external institutions in the beginning of the measure but became obligatory by the end of 2004.

Business foundation allowance

The business foundation allowance of today is paid for nine months to unemployed who intend to become self-employed. This depends on the following conditions:

- The person is unemployment benefit I recipient and is entitled for the benefits for a minimum period of 90 days.
- The person is able to show that he/she possesses the needed knowledge and ability to become self-employed. A business plan needs to be certified by an adequate authority as for example chambers, business associations, banks or other institutions.
- Self-employment needs to be the main economic activity of the person.

The subsidy includes the unemployment benefits and additional €300 for social

insurance contributions. The €300 can be prolonged for further six months if the beneficiary demonstrates economic activity.

Entry allowance

The entry allowance is a subsidy for unemployment benefit II recipients and can be paid up to 24 months. If and how much support is granted is decided by the personal contact person at the agencies of labour. The basic amount depends on the monthly benefits, duration of unemployment and size of household. The main condition to receive the entry allowance is that the person becoming self-employed executes the self-employment as main economic activity.

2.2. Promotion of business-creation

Support of self-employment has a long tradition in Germany. This comprises beside others several information platforms by Federal Ministry of Economics and Technology (BMWi), the Federal Agency of Labour and the Chamber of Industry and Commerce which offer target-oriented knowledge, lectures and personal support for founders. Moreover, there exist several funding models for founders, young companies and small and medium sized enterprises. Recently a new initiative was established by the BMWi to increase the amount of self-employed.

Promotion of business creation by the BMWi

In 2010 an initiative has been developed by the BMWi which is called “Foundation country Germany”. This aims to increase the amount of German business start-ups and comprises measures to strengthen self-employment. The initiative is supported by the Association of German Chambers of Industry and Commerce (DIHK), the German Crafts Association (ZDH) and the Federal Association of Freelancers (BfB) and started in the beginning of 2010. The initiative comprises four action areas:

- Expanded supply of information and actions to increase the willingness to become self-employed and to raise the attractiveness of self-employment
- Target-oriented measures in schools and at universities to impart self-employment as additional option for work
- Improved funding, especially to counteract the current credit crunch
- Improved information for successions of company owners

Funding (also by stimulus packages)

Business starters and small and medium sized (SME) enterprises do not receive the same favourable conditions by banks as large scaled businesses if they raise a bank credit. Therefore, the Federal State offers several promotion programmes for this group of companies:³

- Entry fee by the KfW Mittelstandsbank up to €50,000. The KfW bank is then liable for 80 % of the debt. The loan can be given for a period of three years after foundation.
- ERP⁴ capital for business start-ups fosters sub-ordinated loans. The loan can be up to € 500,000 but only between 45 and 50 % of the needed investment quantity can be offered at the maximum.
- Capital support is given to companies which exist longer than three years. The loan consists of 50 % from the house bank and a sub-ordinated loan from the KfW bank. The loan can be up to €4 millions.
- Enterprise loans by the KfW bank up to an amount of €10 millions for long-term investments. The loan can cover 100 % of the investment costs.
- The KfW Special Programme 2009 was established in the course of the financial crisis and bundled the stimuli packages of the Federal Government. The programme is limited until the end of 2010 and fosters loans up to a limit of €50,000 with an exemption from liability for 90 % of funding regarding investments and 60 % of funding regarding equipment. The promotion was aimed to counteract the credit crunch and comprises all in all around €15 billion.⁵

2.3. Evaluation of measures

Participation

The total amount of people being self-employed constantly rose in the last two decades, all in all by 39 % between 1991 and 2009. Around 4.2 million people were self-employed in 2009. Thereby men are stronger represented than women. In 2009 69 % of self-employed were men and 31 % were women. Even if the higher share of men in the labour force is considered (55 % men and 45 % women in 2009) it is

³ BMWi 2010

⁴ ERP = European Recovery Program

⁵ Bundesministerium für Finanzen [[web](#)]

nevertheless more likely that men start their own business than women.

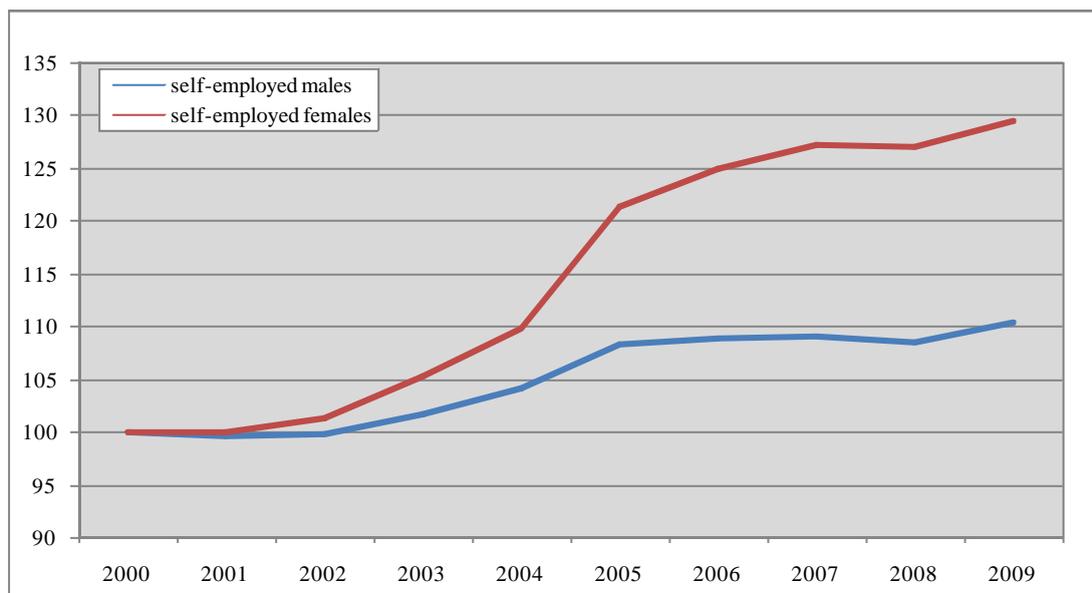
Self-employed are strongly represented in services sector (73 %). Around 20 % work in the manufacturing sector and 7 % in agriculture and forestry sector and fishery. This also shows the increasing tertiarisation of the German economy.⁶

More than half of the self-employed are between 35 and 55 years old (61.5 %). A lower share is between 25 and 35 years old (12.4 %) or between 55 and 60 years old (11.3 %). It is more likely that people aged over 60 years are still self-employed (13.1 %). Among young people between 20 and 25 only 1.4 % started their own business and even less among the 15 to 20 years old – only 0.1 %. This means that self-employed still have to (or want to) work in higher ages. In comparison 4.3 % of the employees are older than 60 years and only 1 % older than 65.

The number of self-employed increased substantially with the introduction of the start-up grant for unemployed in 2003 (Chart 1). Compared to 2000, the amount of women becoming self-employed rose stronger than the amount of men. The number of self-employed also rose between 2008 and 2009. Thus there is no negative impact visible caused by the financial crisis.

Chart 1 Self-employment by gender

2000=100



Source: Statistisches Bundesamt

⁶ Statistisches Bundesamt 2009

There is also a special trend visible comparing the number of self-employed with and without employees: It shows that more than half of the self-employed have no employees (2009: 56 %). The amount increased compared to the pre-Hartz-reform period in 2002 by around 5 percentage points. The number of self-employed men with and without employees stayed quite equal at 51 % without and 49 % for those with employees. Self-employed women on the other hand are more likely to be solo-self-employed. In 2009 66 % of the female self-employed had no employees.

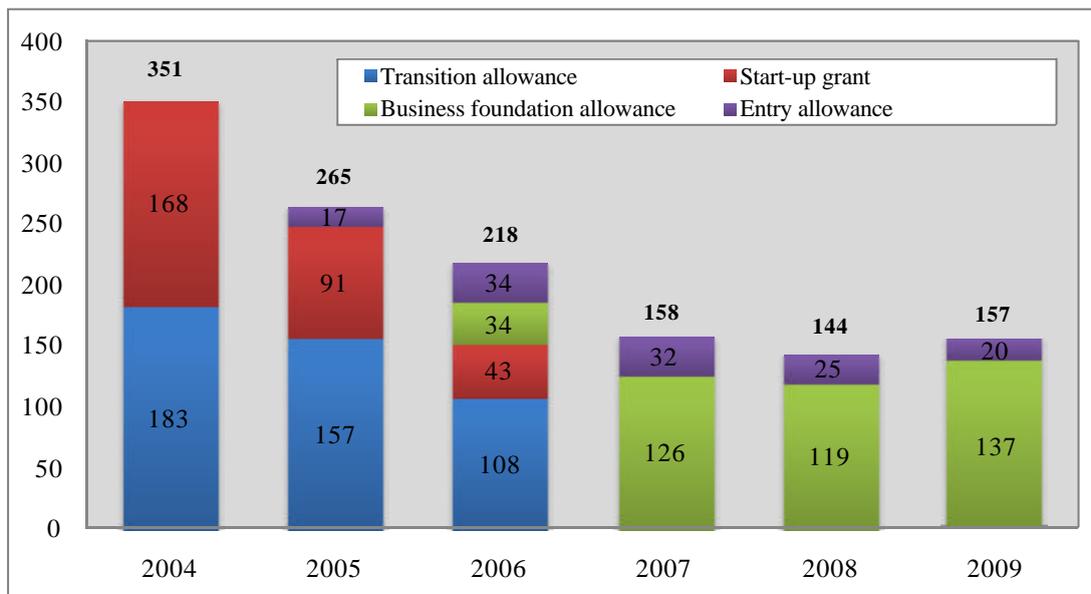
Number of promoted unemployed

The number of promoted unemployed by several measures between 2004 and 2009 is illustrated in Chart 2. It is obvious that the number of promoted self-employment steadily decreased between 2004 and 2008. The decline can probably be attributed to the merge of transition allowance and start-up grant in the foundation business allowance.

The number of promoted self-employment slightly increased between 2008 and 2009 and continued to grow in the first 5 months of 2010. Altogether, 78,000 business start-ups were already promoted this year which equals of an increase of 18 % compared to 2009.

Chart 2 Self-employment by promotion measure

Thousand participants per year



Source: IfM Bonn

Expenditures for promotion

The expenditures of the Federal Agency of Labour for the promotion of self-employment for unemployed aggregated to €1.58 billion in 2009. The expenditures constantly declined since 2005 – all in all by 51 % between 2005 and 2009 (Table 1). €1.56 billion were used for the promotion of the business foundation allowance and €22.8 million for the last beneficiaries of the start-up grant which finally phased out in May 2009.

Table 1 Expenditures for the promotion of self-employment

	2002	2004	2005	2006	2007	2008	2009
Expenditures for the promotion of self-employment (€bn)	1.01	2.73	3.20	2.58	1.82	1.78	1.64
...thereof							
Transition allowance	100%	64%	58%	57%	5%	-	-
Start-up grant	-	36%	42%	40%	28%	9%	1%
Business foundation allowance	-	-	-	3%	67%	91%	99%

Source: Federal Agency of Labour, *Economix*

Evaluation of the transition allowance and the start-up grant

More than 1 million business start-ups, thereof 400,000 Ich AG's, were subsidised between 2003 and 2006. Several studies showed a positive result for the integration of unemployed and their income (Caliendo 2007, IAB et al. 2006). These evaluations revealed that there were strong selection effects. For the transition allowance the beneficiaries are more often men than women and had a better qualification level. For the start-up grant the amount of women was higher compared to the average founder and skills level was generally lower. This was mainly caused by the structuring of the both measures.

The long term effects of both measures – five years after the start-up grant programme started – were investigated by Caliendo (2008) highlighting the following results:

- Between 57 and 63 % of start-up grant's beneficiaries and between 56 and 70 % of transition allowance's beneficiaries were still self-employed after 5 years. The number of drop-outs was stronger for women than men and for East Germany than the West.

- Between 8 and 12 % of those who received the start-up grant were registered as unemployed and between 16 and 21 % were in registered employment. The remaining 7 to 17 % were not specified.
- Between 3 and 10 % who received the transition allowance were unemployed and between 20 and 24 % were in registered employment. The remaining 3 to 11 % were not specified.
- Between 8 and 15 % of former start-up grant recipients dropped-out from self-employment between the third and fifth year. This means these were dependent on the benefits.
- The amount of self-employed working full-time (more than 35 hours per week) lies between 76 and 92 % for men and between 47 and 79 % for women while the number is higher in East Germany compared to the West.
- On average self-employed men have a higher income as women whereby the income is also higher in West Germany than in the East. West German women working less than 15 hours are more often self-employed for additional income and have a net income of around €400-500 per month. Men from West Germany who are working in full-time have the highest net income of around € 2,045 (start-up grant recipients) and € 2,680 (transition allowance recipients).
- The income of self-employed lies on average above the equivalence income.
- Both promotion measures have positive employment effects: by the promotion of 100,000 transition allowances, 80,000 additional full-time equivalent jobs could be created and by the start-up subsidy 16,000 jobs were made up.

A scientific study to assess the business foundation allowance does not yet exist.

3. Quality of self-employment

3.1. Quality at work

Sustainability of foundations

Between 65 and 75 % of all businesses still exist three years after foundation.⁷ The likelihood of existence rises with the amount of funding (> €25.000) and the number of employees. Self-employed promoted by the Federal Agency of Labour have a continuation rate of around 67 % for women and 68 % for men 2.5 years after foundation.⁸ Five years after foundation between 56 and 67 % of the promoted self-employed were still active. The amount of drop-outs mainly increased for the recipients of the start-up grant.

Hours worked

In 2009 self-employed worked 46.3 hours on average per week. The number of hours worked declined constantly in the last decades. In 2003 49.7 hours were still worked on average. Compared to employees who worked 37.8 hours on average in 2008 and 39.2 in 2003 the amount of hours worked decreased by 6.8 % for self employed and by 3.5 % for employees.

Maternity leave and sickness

Maternity leave is protected for employees from 6 weeks before expected birth and 8 weeks after birth. During this period mothers receive 70 % of the net income as maternity benefit.

Self-employed women have only limited possibilities to receive public benefits. One possibility is a voluntary membership in the public health insurance. Under these conditions, self-employed women get the same benefits as employees. The new parents' allowance also grants for income compensation during the early age of the child which seems to have improved the situation for self-employed mothers.

Self-employed persons can protect privately against the income risk of sickness through daily sickness remuneration. The level of benefits can be determined individually.

⁷ KfW 2009

⁸ Caliendo 2008, pp. 7-8

3.2. Flexicurity framework

Self-employed are not eligible to the public insurance system including the public pension insurance and unemployment insurance. They do not pay contributions but also do not receive benefits. Thus the self-employed cover the risk of unemployment by own resources.

The promotion of unemployed into self-employment however supports the self-employed in the foundation phase by unemployment benefits and additional payments for social insurance contributions. It raises on one hand the success of foundation and on the other hand it provides income protection and social insurance as the self-employed can return into benefited unemployment schemes⁹ if the business needs to be abandoned. This instrument can therefore be seen as flexicurity instrument.

In order to lower the risk of unemployment, self-employed can become a member of the unemployment insurance on a voluntary basis but only those coming from previous registered employment or unemployment.

Moreover, they have the possibility to become a member of the public pension insurance. In 2008 around 39 % voluntarily paid into the public pension insurance. This however does not mean that the remaining self-employed do not accumulate resources for the future. They use private pension arrangements or capital investments.

Self-employed are also eligible for social benefits. In particular they are protected against poverty by the basic social income; they receive child allowance like all other parents and get the lately implemented parent s' allowance.

3.3. Impact of the financial crisis

Around 48 % of young founders – founders between 2005 and 2008 – were affected by the negative impacts of the financial crisis while 9 % could gain

⁹ As long as the entitlement exists. The entitlement is valid until four years after foundation, whereby the total amount of benefits – business foundation allowance plus received unemployment benefit I – can together only total to 12 month.

from the financial crisis.¹⁰ They are mainly influenced by the order situation, volume of sales and profits. 41 % reported declines of orders and 8 % had larger orders. The same trend is shown for the decrease of volumes and profits (43 % and 49 % respectively) and increase of volumes and profits (7 % for both).

According to the KfW-Gründungsmonitor 2009 around 71 % of all self-employed need resources for funding of investments and equipment. 34 % of these use external sources and 27 % use both external and own sources for funding. The remaining 66 % solely use own sources. While in 2008 the majority of founders did not have any problems with funding, 17 % had problems with funding in the context of foundation and 7 % of these did not receive a bank credit. This was however no difference to previous years and is thus not impacted by the financial crisis.

3.4. Transition and income trends

Transition

The number of foundations rose between 2002 and 2004 and is since then decreasing (Chart 3). The number of liquidations developed almost in the same direction. In 2008 the amount of liquidations exceeded business foundations by around 12,000. This was mainly caused by the financial crisis due to stronger insolvency and illiquidity. In 2009 the balance was positive again.

The highest amount of new foundations starts their economic activity within the services sector (83 %). The remaining foundations take place in the manufacturing sector (3 %), in the construction sector (7 %) and in non-service sectors¹¹ (75%).¹²

Income

The net income profile of self-employed was almost equal between 2002 and 2008. There was a slight decrease in income groups with net incomes above 1,100 per month and an increase in income groups below this level respectively between 2002 and 2006. This was influenced by the strong increase of foundations without employees as a result of the start-up grant. In 2006 only 1/3 of all business start-ups was undertaken with employees.

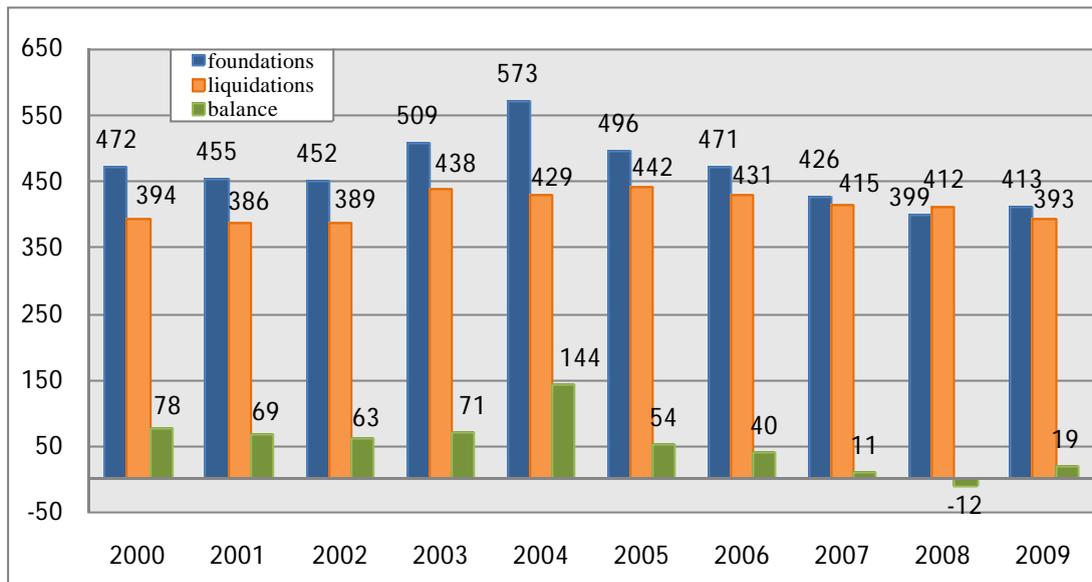
¹⁰ KfW/ZEW 2009

¹¹ Non-services sectors comprise agriculture, forestry and fishery as well as renewable energies

¹² KfW 2010

Chart 3 Number of business foundations and liquidations

In thousands

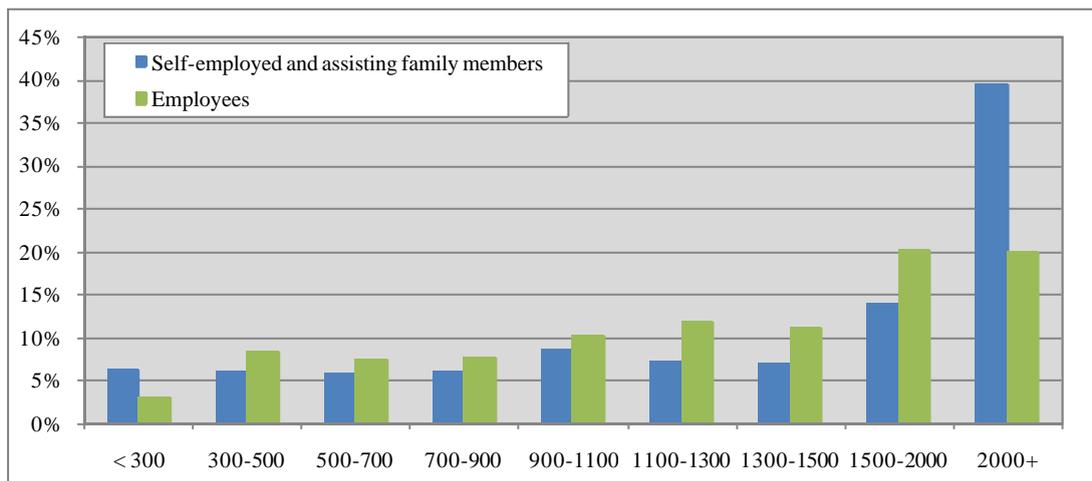


Source: IfM Bonn

The different distribution of monthly net income of self-employed and employees is eye catching. Employees are stronger represented in incomes groups below €2,000 than self-employed (Chart 4) while around 40 % of self-employed earn a net income above €2,000 compared to 20 % of employees.

Chart 4 Monthly net income in 2008

% share



Source: Statistisches Bundesamt

3.5. Abuses

Self-employment can be used to avoid paying fees into statutory unemployment insurance, the pension insurance, health insurance and nursing care insurance.

The self-employed are however obliged to be medically insured but they can choose between the statutory and the private health insurance system. Thus people who would be normally dependent employed by their employer become self-employed without changing the work situation and continue to work for their old company/employer – known as disguised employment (*Scheinselbstständigkeit*).

Before 1999 there was no legal basis for disguised employment. This was changed with the law § 7 Abs. 4 SGB IV which determined five criteria to determine disguised employment. These criteria were abolished again in the course of the Hartz-reforms. Nowadays only the statutory pension insurance can charge the self-employed if he/she works only for one employer and has no employees. An assessment procedure is previously required.

4. Conclusions

Self-employment is an important pillar of the German labour force. Self-employed are mostly represented in the services sector which emphasises the tertiarisation of the German economy.

The promotion of unemployed into self-employed is a successful instrument of active labour market policies and adapts the flexicurity approach. Approximately every fifth new founders was previously unemployed. The sustainability of businesses lies between two thirds and three fourths three years after foundation.

In the course of the financial crisis the number of self-employed slightly increased combined with a relatively small rise of promoted unemployed. Thus self-employment was resistant against the economic downturn. Moreover it seems that the attractiveness of self-employment rose, caused by a difficult job situation on the labour market. A combination of job conservation by flexible working schemes on one hand and the simultaneous absence of job supply on the other hand seemed to be at work.

Self-employed have on average a higher income than employees but also have to cover the business risk by own resources. The highest risk emerges from unemployment. Self-employed only have limited access to public

unemployment insurance. For self-employed mothers the income loss from maternity leave can be compensated by the recently introduced parents' allowance.

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Web links:

IfM Bonn Homepage [[web](#)]